

## NEW ISSUE

In the opinion of Orrick, Herrington & Sutcliffe LLP, Bond Counsel, based upon an analysis of existing laws, regulations, rulings and court decisions, and assuming, among other matters, the accuracy of certain representations and compliance with certain covenants, interest on the Fiscal 2006 AA Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986. In the further opinion of Bond Counsel, interest on the Fiscal 2006 AA Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although Bond Counsel observes that such interest is included in adjusted current earnings when calculating corporate alternative minimum taxable income. Bond Counsel is also of the opinion that interest on the Fiscal 2006 AA Bonds is exempt from personal income taxes imposed by the State of New York and any political subdivision thereof (including The City of New York). Bond Counsel expresses no opinion regarding any other tax consequences related to the ownership or disposition of, or the accrual or receipt of interest on, the Fiscal 2006 AA Bonds. See "TAX MATTERS."

# **\$400,000,000** **New York City** **Municipal Water Finance Authority**

## **Water and Sewer System Second General Resolution Revenue Bonds, Adjustable Rate Fiscal 2006 Series AA**

**consisting of**  
**\$200,000,000 Fiscal 2006 Sub-series AA-1 Bonds**  
**\$100,000,000 Fiscal 2006 Sub-series AA-2 Bonds**  
**\$100,000,000 Fiscal 2006 Sub-series AA-3 Bonds**

**Dated: Date of Delivery**

**Due: June 15, 2032**

The Fiscal 2006 AA Bonds will be issued as registered bonds and will be registered in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York which will act as securities depository for the Fiscal 2006 AA Bonds. Purchases of beneficial interests in such Fiscal 2006 AA Bonds will be made in book-entry-only form. Purchasers will not receive certificates representing the ownership interest in the Fiscal 2006 AA Bonds purchased by them. See "APPENDIX F—BOOK-ENTRY-ONLY FORM."

The Fiscal 2006 AA Bonds will be issued in three Sub-Series. The Fiscal 2006 AA-1 Bonds will be issued in the aggregate principal amount of \$200,000,000 and will bear interest at a Daily Rate unless and until converted to bear interest in a different Rate Mode. The Fiscal 2006 AA-2 Bonds will be issued in the aggregate principal amount of \$100,000,000 and will bear interest at a Daily Rate unless and until converted to bear interest in a different Rate Mode. The Fiscal 2006 AA-3 Bonds will be issued in the aggregate principal amount of \$100,000,000 and will bear interest at a Weekly Rate unless and until converted to bear interest in a different Rate Mode. The interest rate applicable to all or a portion of the Fiscal 2006 AA Bonds may be converted to a Daily Rate, Commercial Paper Rate, Weekly Rate, Flexible Rate or a Fixed Rate. See "THE FISCAL 2006 AA BONDS—Conversion to an Alternate Rate Period." Interest accruing during a Daily Rate Period or a Weekly Rate Period will be payable on the 15th day of each calendar month. Interest accruing during a Flexible Rate Period or the Fixed Period will be payable on June 15 and December 15 of each year. Interest accruing during a Commercial Paper Rate Period of 270 days or less will be payable on the Reset Date. Interest accruing during a Commercial Paper Rate Period of more than 270 days will be payable on the next succeeding Reset Date or Conversion Date and the date which is 180 calendar days prior to such Reset Date or Conversion Date. Fiscal 2006 AA Bonds subject to a Daily Rate Period, a Commercial Paper Rate Period or a Weekly Rate Period will be issuable in Authorized Denominations of \$100,000 or integral multiples of \$5,000 in excess thereof and the Fiscal 2006 AA Bonds subject to a Flexible Rate Period or the Fixed Rate Period will be issuable in Authorized Denominations of \$5,000 or integral multiples thereof. The Fiscal 2006 AA Bonds bearing interest at a Daily Rate or a Weekly Rate may be tendered to the Tender Agent for purchase at the option of the Owner thereof under the circumstances described herein. The Fiscal 2006 AA Bonds are also subject to mandatory tender and to redemption prior to maturity, as described herein. Liquidity support for the payment of the Purchase Price of tendered but unremarketed Fiscal 2006 AA-1 Bonds is provided, on a several basis as described herein, by State Street Bank and Trust Company and California State Teachers' Retirement System under a Standby Bond Purchase Agreement with the Authority. Liquidity support for the payment of the Purchase Price of tendered but unremarketed Fiscal 2006 AA-2 and Fiscal 2006 AA-3 Bonds is provided by Dexia Crédit Local, acting through its New York Branch, under a Standby Bond Purchase Agreement with the Authority. The obligations of such Liquidity Providers are subject to immediate termination or suspension without notice upon the occurrence of certain events described herein.

The proceeds of the Fiscal 2006 AA Bonds are expected to be applied (i) to pay principal and interest on a portion of the Authority's Outstanding Commercial Paper Notes, (ii) to fund a portion of the Authority's capital program and (iii) to pay certain costs of issuance.

**The Fiscal 2006 AA Bonds are special obligations of the Authority, payable solely from and secured by a pledge of and subordinate lien on the gross revenues of the System. The Authority has no taxing power. The Fiscal 2006 AA Bonds are not a debt of the State of New York, The City of New York or the New York City Water Board and none of the State of New York, The City of New York or the New York City Water Board is liable on the Fiscal 2006 AA Bonds.**

The Fiscal 2006 AA Bonds are offered when, as and if issued by the Authority and received by the Underwriters, and subject to the approval of legality by Orrick, Herrington & Sutcliffe LLP, New York, New York, Bond Counsel. Certain legal matters will be passed upon for the Underwriters by Nixon Peabody LLP, New York, New York. Certain legal matters will be passed upon for State Street Bank and Trust Company by King & Spalding LLP. Certain legal matters will be passed upon for California State Teachers' Retirement System by Fulbright & Jaworski L.L.P. Certain legal matters will be passed upon for Dexia Crédit Local, acting through its New York Branch, by King & Spalding LLP and by Jeantet & Associates. It is anticipated that the Fiscal 2006 AA Bonds will be available for delivery to The Depository Trust Company in New York, New York, on or about October 27, 2005.

**GOLDMAN, SACHS & CO.**  
as Underwriter and  
Remarketing Agent of the  
Fiscal 2006 AA-1 Bonds

**BANC OF AMERICA SECURITIES LLC**  
as Underwriter and  
Remarketing Agent of the  
Fiscal 2006 AA-2 Bonds

**LOOP CAPITAL MARKETS, LLC**  
as Underwriter and  
Remarketing Agent of the  
Fiscal 2006 AA-3 Bonds

**PRINCIPAL AMOUNTS, RATE MODES AND PRICES**

**\$400,000,000  
New York City  
Municipal Water Finance Authority**

**Water and Sewer System Second General Resolution Revenue Bonds,  
Adjustable Rate Fiscal 2006 Series AA**

**Price: 100%**

**\$200,000,000 Fiscal 2006 AA-1 Bonds**

Rate Mode: Daily Rate

First Interest Payment Date: November 15, 2005

Remarketing Agent: Goldman, Sachs & Co.

Facility Providers: State Street Bank and Trust Company and California State Teachers'  
Retirement System (each severally obligated for 50% of amounts payable)

**\$100,000,000 Fiscal 2006 AA-2 Bonds**

Rate Mode: Daily Rate

First Interest Payment Date: November 15, 2005

Remarketing Agent: Banc of America Securities LLC

Facility Provider: Dexia Crédit Local, acting through its New York Branch

**\$100,000,000 Fiscal 2006 AA-3 Bonds**

Rate Mode: Weekly Rate

First Interest Payment Date: November 15, 2005

Remarketing Agent: Loop Capital Markets, LLC

Facility Provider: Dexia Crédit Local, acting through its New York Branch

**New York City Municipal Water Finance Authority**  
**75 Park Place, 6th Floor**  
**New York, New York 10007**  
**212-788-5889**

Mark Page, <i>ex officio</i>	<i>Member</i>
Denise Sheehan, <i>ex officio</i>	<i>Member</i>
Martha E. Stark, <i>ex officio</i>	<i>Member</i>
Emily Lloyd, <i>ex officio</i>	<i>Member</i>
Charles E. Dorkey III	<i>Member</i>
Arthur B. Hill	<i>Member</i>
Peter J. Kenny	<i>Member</i>
Alan L. Anders	<i>Executive Director</i>
Marjorie E. Henning	<i>Secretary</i>
George Zoukee	<i>Treasurer</i>
Lawrence R. Glantz	<i>Comptroller</i>
Michele Mark Levine	<i>Deputy Comptroller</i>
Philip Wasserman	<i>Deputy Treasurer</i>
Prescott D. Ulrey	<i>Assistant Secretary</i>
Jeffrey M. Werner	<i>Assistant Secretary</i>
Raymond Orlando	<i>Manager of Investor Relations</i>

**New York City Water Board**  
**59-17 Junction Boulevard, 8th Floor**  
**Flushing, New York 11373-5108**  
**718-595-3586**

James T.B. Tripp	<i>Chair</i>
Lilyan H. Affinito	<i>Member</i>
Donald Capoccia	<i>Member</i>
Dawn S. Davis	<i>Member</i>
Amaziah Howell	<i>Member</i>
Stacey Coleman Morse	<i>Member</i>
Maria Santos Valentin	<i>Member</i>
David B. Tweedy	<i>Executive Director</i>
William Kusterbeck	<i>Treasurer</i>
Carmelo Emilio	<i>Deputy Treasurer</i>
Albert F. Moncure, Jr.	<i>Secretary</i>

**Authority Consultants**

Bond Counsel	<i>Orrick, Herrington &amp; Sutcliffe LLP</i>
Consulting Engineer	<i>Metcalf &amp; Eddy of New York, Inc.</i>
Financial Advisors	<i>Lamont Financial Services Corporation/Ramirez &amp; Co., Inc.</i>
Rate Consultant	<i>Amawalk Consulting Group LLC</i>

This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy any of the Fiscal 2006 AA Bonds in any jurisdiction to any person to whom it is unlawful to make such offer in such jurisdiction. No dealer, salesperson or any other person has been authorized to give any information or make any representation, other than those contained herein, in connection with the offering of any of the Fiscal 2006 AA Bonds and if given or made, such information or representation must not be relied upon. Information contained on the Authority's web page, on the City's web site, or on any other web page is not a part of this Official Statement. Neither the delivery of this Official Statement nor the sale of any of the Fiscal 2006 AA Bonds implies that there has been no change in the affairs of the Authority, the Board or the City or the other matters described herein since the date hereof.

If and when included in this Official Statement, the words "expects," "forecasts," "projects," "intends," "anticipates," "estimates" and analogous expressions are intended to identify forward-looking statements as defined in the Securities Act of 1933, as amended, and any such statements inherently are subject to a variety of risks and uncertainties that could cause actual results to differ materially from those projected. Such risks and uncertainties include, among others, general economic and business conditions, changes in political, social and economic conditions, regulatory initiatives and compliance with governmental regulations, litigation and various other events, conditions and circumstances, many of which are beyond the control of the Authority. These forward-looking statements speak only as of the date of this Official Statement. The Authority disclaims any obligation or undertaking to release publicly any updates or revisions to any forward-looking statement contained herein to reflect any change in the Authority's expectations with regard thereto or any change in events, conditions or circumstances on which any such statements are based.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITERS MAY OVERALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF THE FISCAL 2006 AA BONDS AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

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## SUMMARY STATEMENT

*The following is a brief summary of the information contained in this Official Statement and is subject in all respects to the additional information contained herein, including the appendices attached hereto. Defined terms have the same meaning herein as elsewhere in this Official Statement.*

**Use of Proceeds:** The Fiscal 2006 AA Bonds are being issued to (i) pay principal and interest on all or a portion of the Authority's Commercial Paper Notes, Series One and Series Five, (ii) fund a portion of the Authority's capital program and (iii) pay certain costs of issuance.

**Description of the Bonds:** The Fiscal 2006 AA Bonds are being issued by the Authority in the principal amount of \$400,000,000 pursuant to its Water and Sewer System Second General Revenue Bond Resolution adopted on March 30, 1994, as amended (the "Second Resolution"), and its Supplemental Resolution No. 37 adopted on September 26, 2005.

**The System:** The Water System provides approximately 1,220 million gallons per day (mgd) of water to approximately 824,000 accounts. It supplies water to approximately 9,000,000 people, of which approximately 8,000,000 are in the City and the balance are in Westchester, Putnam, Orange and Ulster Counties. The Sewer System is comprised of an extensive network of sewage collection and treatment facilities that treat over 1,300 mgd of wastewater. Under the Act, the Lease and the Agreement, the Board is obligated to pay the operating expenses of the System. The City is obligated to operate and maintain the System regardless of payment by the Board.

Summary Financial Information:	Historical			Projected (1)		
	FY 2002	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007
	(Millions of Dollars)					
Revenues Available for Debt Service (2) . . .	\$1,592.4	\$1,653.7	\$1,759.3	\$1,746.1	\$1,980.6	2,059.7
Other Revenues (2) . . . . .	31.0	99.1	30.6	—	—	—
Net Operating Expenses (2) . . . . .	708.3	782.4	777.5	987.3	944.6	908.9
Other Expenses (including Rental Payments to New York City) (2) . . . . .	172.2	263.3	332.1	106.2	187.7	224.7
Total Expenses (2) . . . . .	880.5	1,045.7	1,109.6	1,093.5	1,132.3	1,133.6
Total First Resolution Bond Debt Service . .	496.4	496.7	490.3	473.0	551.4	640.9
Net Debt Service on Second Resolution Bonds (3) . . . . .	—	—	—	58.4	171.0	191.0
Net Surplus . . . . .	246.0	210.4	190.0	121.2	126.0	94.2
First Resolution Debt Service Coverage . . .	3.20x	3.33x	3.59x	3.69x	3.59x	3.21x
First and Second Resolution Debt Service Coverage (3) . . . . .	3.20x	3.33x	3.59x	3.29x	2.74x	2.48x
Rate Increase . . . . .	3.0%	6.5%	5.5%	5.5%(4)	3.0%(5)	5.6%

Totals may not add due to rounding.

- (1) Projections are as of April 2005.
- (2) Historical figures are derived from the accounting records utilized in preparation of the statements of cash flows contained in the annual financial statements.
- (3) Includes interest on Commercial Paper Notes and reflects offset of carryforward revenues.
- (4) Actual rate increase for Fiscal Year 2005.
- (5) Actual rate increase for Fiscal Year 2006.

**Total Authority Debt Outstanding:** As of the date of this Official Statement, the Authority has approximately \$10.1 billion of First Resolution Bonds (defined below) and \$4.2 billion of Second Resolution Bonds (defined below) Outstanding. See “CAPITAL IMPROVEMENT AND FINANCING PROGRAM—Debt Service Requirements.” In addition, the Authority currently has an \$800 million commercial paper program.

**Capital Program:** The City’s Ten Year Capital Strategy published in June 2005 (the “Ten Year Capital Strategy”), which is updated every two years, includes the projected capital improvements to the System for Fiscal Years 2006 through 2015. The City’s Current Capital Plan (the “Current Capital Plan”), which was published in June 2005 and covers Fiscal Years 2006 through 2009, is updated quarterly and is consistent with the Ten Year Capital Strategy for Fiscal Years 2006 through 2009. The Ten Year Capital Strategy as modified by the Current Capital Plan comprises the Capital Improvement Program (the “CIP”). The CIP is designed to maintain a satisfactory level of service, to improve operation of the System and to address future System requirements.

**Bond Financing Program:** The following table shows total Authority indebtedness expected to be issued for capital purposes, excluding refunding bonds, from Fiscal Year 2006 to Fiscal Year 2010, as of April 2005.

<u>FY 2006</u>	<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>	<u>FY 2010</u>	<u>Period Total</u>
(Millions of Dollars)					
\$1,687.4	\$1,681.3	\$1,754.6	\$1,717.6	\$1,602.3	\$8,443.2

**Security for the Second Resolution Bonds:**

**Revenue Pledge:** The Second Resolution Bonds are special obligations of the Authority, payable solely from and secured by a pledge of amounts on deposit in the Subordinated Indebtedness Fund established under the General Resolution and all moneys and securities in the funds and accounts established under the Second Resolution, except the Arbitrage Rebate Fund and the Debt Service Reserve Fund, the gross revenues of the System prior to the payment of operation and maintenance costs or any other expenses.

**Debt Service Reserve Fund:** The Fiscal 2006 AA Bonds will not be secured by a Debt Service Reserve Fund.

**Rate Covenant:** The Board has covenanted to establish and collect rates, fees and charges sufficient in each Fiscal Year so that Revenues collected in such Fiscal Year will be at least equal to the sum of 115% of Aggregate Debt Service on all First Resolution Bonds Outstanding and on any Projected Series of First Resolution Bonds (excluding Refundable Principal Installments for the



payment of which funds are held in trust) payable in such Fiscal Year, and 100% of the Operating Expenses and Required Deposits (which includes debt service on the Second Resolution Bonds and other subordinate debt) to the extent required to be paid from Revenues for such Fiscal Year.

**Additional Bonds Test:**

Additional Second Resolution Bonds secured on a parity with the Fiscal 2006 AA Bonds, may be issued under the Second Resolution to pay for capital improvements to the System and to refund First Resolution Bonds, Second Resolution Bonds, commercial paper notes issued by the Authority and general obligation bonds of the City issued for water and sewer purposes. Additional Second Resolution Bonds may be issued subject to financial tests specified in the Second Resolution. Additional First Resolution Bonds may be issued under the First Resolution which would have a first lien on amounts on deposit in the Subordinated Indebtedness Fund prior to the lien securing Second Resolution Bonds.

**Rates:**

Rates, fees and charges are imposed by the Board and are not subject to regulatory approval except for those rates charged to a limited class of upstate users representing approximately 1% of Revenues.

**The Authority:**

The Authority, a separate legal entity established in 1984, has the power to (i) issue bonds, bond anticipation notes and other obligations for the purpose of financing the renovation and improvement of the System, (ii) refund its bonds and notes and general obligation bonds of the City issued for water or sewer purposes, (iii) require the Board to fix rates sufficient to pay the costs of operating and financing improvements to the System and (iv) require the City to maintain the System adequately. The Authority has no taxing power.

**The Board:**

The Board, a separate legal entity established in 1984, has leased the System from the City. It is authorized to fix and collect rates, fees and charges adequate to pay the cost of operating and financing the System.

**The Agreement:**

Pursuant to the Agreement, the Authority has agreed to finance capital projects for the System, both current work and work commenced in prior years, through the issuance of bonds, notes or other indebtedness secured by revenues of the System.

**The Lease:**

Pursuant to the Lease, the Board has acquired the System from the City for a term continuing until provision has been made for the repayment of all Outstanding Bonds or other indebtedness of the Authority.

Financial Statements and Independent  
Auditors:

The financial statements of the System as of and for the year ended June 30, 2004 included in Appendix D to this Official Statement have been audited by Grant Thornton LLP, independent auditors, as stated in their report appearing therein.

## OFFICIAL STATEMENT

\$400,000,000

### NEW YORK CITY MUNICIPAL WATER FINANCE AUTHORITY WATER AND SEWER SYSTEM SECOND GENERAL RESOLUTION REVENUE BONDS, FISCAL 2006 SERIES AA

#### INTRODUCTORY STATEMENT

##### General

The purpose of this Official Statement is to set forth certain information pertaining to the New York City Municipal Water Finance Authority (the “Authority”), a public benefit corporation duly created and existing under the New York City Municipal Water Finance Authority Act, as amended (the “Act”); the New York City Water Board (the “Board”), a public benefit corporation created and existing under Chapter 515 of the Laws of 1984, both of which laws were enacted by the Legislature of the State of New York (the “State”); and the Authority’s \$400,000,000 Water and Sewer System Second General Resolution Revenue Bonds, Fiscal 2006 Series AA (the “Fiscal 2006 AA Bonds”) consisting of \$200,000,000 Fiscal 2006 Sub-Series AA-1 Bonds (the “Fiscal 2006 AA-1 Bonds”), \$100,000,000 Fiscal 2006 Sub-Series AA-2 Bonds (the “Fiscal 2006 AA-2 Bonds”) and \$100,000,000 Fiscal 2006 Sub-Series AA-3 Bonds (the “Fiscal 2006 AA-3 Bonds”). Capitalized terms used in this Official Statement and not defined herein shall have the meanings ascribed thereto in APPENDIX C—GLOSSARY AND SUMMARY OF CERTAIN DOCUMENTS—Glossary.”

Pursuant to a lease agreement (the “Lease”) between the Board and The City of New York (the “City”), dated as of July 1, 1985, as amended, the Board has leased from the City its facilities for the collection, transmission and distribution of water (the “Water System”) and its facilities for the collection, treatment and disposal of sewage (the “Sewer System”) (collectively, the “System”). As required by the Act and the Lease, the System is operated and maintained by the Department of Environmental Protection of the City (“DEP”). The Board has also entered into a financing agreement, dated as of July 1, 1985, as amended (the “Agreement”), with the Authority and the City for the financing of capital improvements to the System through the issuance of bonds, notes and other obligations (the “First Resolution Bonds”) under the Authority’s Water and Sewer System General Revenue Bond Resolution adopted on November 14, 1985, as amended (the “First Resolution”), or subordinate obligations of the Authority under its Second Resolution (defined below). Pursuant to the Lease and the Agreement, the Board has agreed to levy and collect rates, fees and charges. Pursuant to the Lease, the City may, with the prior written consent of the Board, grant interests in the Leased Property which, in the reasonable judgment of the Board, do not interfere with the operation and maintenance of the System and the collection of the Revenues from the System.

The Fiscal 2006 AA Bonds will be issued by the Authority pursuant to its Water and Sewer System Second General Revenue Bond Resolution, adopted on March 30, 1994, as amended (the “Second Resolution”) and its Supplemental Resolution No. 37 adopted on September 26, 2005 (the “Supplemental Resolution”). All bonds issued under the Second Resolution are referred to herein as “Second Resolution Bonds.” The Second Resolution and the Supplemental Resolution are collectively referred to herein as the “Resolutions.” The Bank of New York serves as trustee under the Resolutions (in such capacity, the “Trustee”) and will continue to serve as Trustee unless a successor is appointed in accordance with the Resolutions. The Bank of New York also serves as trustee under the First Resolution.

The Second Resolution Bonds are special obligations of the Authority, payable solely from and secured by a pledge of amounts on deposit in the Subordinated Indebtedness Fund established by the First Resolution and all moneys or securities in any of the funds and accounts established under the Second Resolution, subject only to provisions of the Second Resolution and the Agreement relating to the use and application thereof. The Board has covenanted in the Agreement to maintain rates, fees and charges at sufficient levels to produce in each twelve-month period beginning on July 1 (a “Fiscal Year”) an amount equal to 115% of the Aggregate Debt Service and Projected Debt Service on the First Resolution Bonds (excluding Refundable Principal Installments for the payment of which funds are held

in trust) to become due in such Fiscal Year on First Resolution Bonds, plus 100% of the operation and maintenance expenses of the System certified by the City and of Required Deposits (which includes the debt service on the Second Resolution Bonds and other subordinate debt) to the extent required to be paid from Revenues. The Agreement requires a report of the Rate Consultant setting forth its recommendations as to any revisions of the rates, fees and charges necessary or advisable to meet the requirements of the rate covenant. The Board is obligated to take necessary action to cure or avoid any deficiency. See "SECURITY FOR THE SECOND RESOLUTION BONDS—Rate Covenant." The Agreement also requires a Consulting Engineer to review the operation and maintenance of the System, and further requires the City to operate and maintain the System in accordance with the advice and recommendations of the Consulting Engineer. See "SECURITY FOR THE SECOND RESOLUTION BONDS."

Rates, fees and charges are imposed by the Board and are not subject to regulatory approval under current law except for the rates charged to a limited class of upstate users, representing approximately 1% of Revenues. See "RATES AND BILLINGS."

The Authority has relied upon Metcalf & Eddy of New York, Inc. ("Metcalf & Eddy"), its Consulting Engineer, for certain engineering feasibility information and upon Amawalk Consulting Group LLC ("Amawalk Consulting"), its Rate Consultant, for certain financial estimates and projections. See "ENGINEERING FEASIBILITY REPORT AND FORECASTED CASH FLOWS."

### **Financial Projection Assumptions**

The estimates and projections contained in this Official Statement are based on, among other factors, evaluations of historical revenue and expenditure data and analyses of economic trends affecting the Authority's finances. The financial projections contained herein are subject to certain contingencies that cannot be quantified and are subject to the uncertainties inherent in any attempt to predict the results of future operations. Accordingly, such projections are subject to periodic revision which may involve substantial change. Consequently, the Authority makes no representation or warranty that these estimates and projections will be realized.

The financial projections contained in this Official Statement, including projected bond financing, projected operating and maintenance expenses, debt service, revenues, sources and uses of funds, and the forecasted cash flows and rate increases, were prepared in April 2005 and are expected to be updated annually. Based on results to date and other factors, actual financial results will differ from these projections.

The audited financial results for Fiscal Year 2005 were not available as of the date of this Official Statement. The preliminary results indicate that the surplus for Fiscal Year 2005 was \$159 million on a cash basis.

## USE OF PROCEEDS

It is anticipated that the proceeds of the Fiscal 2006 AA Bonds will be applied in the following manner:

Deposit for Payment of Commercial Paper Notes .....	\$376,855,000
Deposit to Construction Fund.....	\$ 22,750,000
Underwriters' Discount.....	\$ 24,000
Costs of Issuance* .....	\$ 371,000

\* Includes fees and expenses of Facility Providers relating to the Standby Purchase Agreements.

## THE FISCAL 2006 AA BONDS

### General

The Fiscal 2006 AA-1 Bonds will be issued in the aggregate principal amount of \$200,000,000 and will bear interest at the Daily Rate unless and until converted to bear interest in a different Rate Mode. The Fiscal 2006 AA-2 Bonds will be issued in the aggregate principal amount of \$100,000,000 and will bear interest at the Daily Rate unless and until converted to bear interest in a different Rate Mode. The Fiscal 2006 AA-3 Bonds will be issued in the aggregate principal amount of \$100,000,000 and will bear interest at the Weekly Rate unless and until converted to bear interest in a different Rate Mode. The interest rate applicable to all or any portion of the Fiscal 2006 AA Bonds may be converted to a Daily Rate, Commercial Paper Rate, Weekly Rate, Flexible Rate, or Fixed Rate. The Fiscal 2006 AA Bonds will mature on June 15, 2032. The Fiscal 2006 AA Bonds are subject to optional and mandatory redemption prior to maturity as described under "Redemption of Fiscal 2006 AA Bonds" and to optional and mandatory tender for purchase as described under "Optional Tender for Purchase" and "Mandatory Tender for Purchase." The Fiscal 2006 AA Bonds will continue in a Rate Period until converted to another Rate Period and will bear interest at a rate determined in accordance with the procedures for determining the interest rate during such Rate Period. See "Conversion to an Alternate Rate Period" and "Interest Rates and Reset Dates" below.

Principal and Purchase Price of, and redemption premium, if any, and interest on, the Fiscal 2006 AA Bonds will be payable in lawful money of the United States of America. The Fiscal 2006 AA Bonds will be issued only as fully registered bonds without coupons in denominations of \$100,000 and integral multiples of \$5,000 in excess thereof when the Rate Period is the Initial Period, a Daily Rate Period, a Commercial Paper Rate Period, or a Weekly Rate Period, and in denominations of \$5,000 and integral multiples thereof when the Rate Period is a Flexible Rate Period or the Fixed Rate. During the Initial Period, a Daily Rate Period, a Commercial Paper Rate Period or a Weekly Rate Period, interest will be computed on the basis of a 365-day or 366-day year for the actual number of days elapsed and during a Flexible Rate Period and the Fixed Rate Period, interest will be computed on the basis of a 360-day year of twelve 30-day months.

The Bank of New York has been appointed as Tender Agent for the Fiscal 2006 AA Bonds. Goldman, Sachs & Co. has been appointed as the Remarketing Agent for the Fiscal 2006 AA-1 Bonds (the "2006 AA-1 Remarketing Agent"). Banc of America Securities LLC has been appointed as the Remarketing Agent for the Fiscal 2006 AA-2 Bonds (the "2006 AA-2 Remarketing Agent"). Loop Capital Markets, LLC has been appointed as the Remarketing Agent for the Fiscal 2006 AA-3 Bonds (the "2006 AA-3 Remarketing Agent" and, together with the 2006 AA-1 Remarketing Agent and the 2006 AA-2 Remarketing Agent, the "Remarketing Agents").

### Record Dates and Interest Payment Dates

*Record Dates.* Interest on the Fiscal 2006 AA Bonds will be payable to the registered owner thereof as shown on the registration books kept by the Trustee at the close of business on the Record Date which will be (i) the immediately preceding Business Day prior to a Bond Payment Date when the Fiscal 2006 AA Bonds are in the Initial Period, a Daily Rate Period, a Weekly Rate Period or a Commercial Paper Rate Period and (ii) the first day (whether or not a Business Day) of the calendar month during which interest thereon is payable for Flexible Rate Periods and the Fixed Rate Period.

*Bond Payment Dates.* Interest on the Fiscal 2006 AA Bonds will be payable on the 15th day of each calendar month when the Fiscal 2006 AA Bonds bear interest at the Initial Rate, a Daily Rate or a Weekly Rate and on June 15 and December 15 of each year when the Fiscal 2006 AA Bonds are in a Flexible Rate Period or the Fixed Rate Period. Interest on the Fiscal 2006 AA Bonds in a Commercial Paper Rate Period comprised of 270 days or less shall be paid on the next succeeding Reset Date or Conversion Date and interest on the Fiscal 2006 AA Bonds in a Commercial Paper Rate Period comprised of more than 270 days shall be paid (i) on the next succeeding Reset Date or Conversion Date and (ii) the date which is 180 calendar days prior to such Reset Date or Conversion Date. If any such day is not a Business Day, then the Bond Payment Date will be the next succeeding Business Day. Interest payable on each Bond Payment Date for Fiscal 2006 AA Bonds bearing interest in the Initial Rate Period, Daily Rate Mode, Commercial Paper Rate Mode or the Weekly Rate Mode shall be the interest accruing and unpaid through and including the day preceding such Bond Payment Date. Interest payable on each Bond Payment Date bearing interest in the Flexible Rate Mode or the Fixed Rate Mode shall be the interest accruing and unpaid through and including the respective June 14th or December 14th preceding such Bond Payment Date.

### **Conversion to an Alternate Rate Period**

At the election of the Authority, all or a portion of a Sub-Series of the Fiscal 2006 AA Bonds may be converted to a Rate Period of a different duration by delivering a notice (the “Conversion Notice”) to the Remarketing Agent for such Sub-Series, the Facility Provider for such Sub-Series, DTC and the Tender Agent specifying, among other things, the new Rate Mode or Modes to which the Fiscal 2006 AA Bonds are then subject and the conversion date (which shall be a Reset Date or a Bond Payment Date) (a “Conversion Date”). The Authority must deliver such Conversion Notice at least fifteen days prior to the Conversion Date (or if the Fiscal 2006 AA Bonds to be converted are Book Entry Bonds, such shorter period as DTC will permit). The Tender Agent is to give written notice to the registered owner of each Fiscal 2006 AA Bond of the Authority’s election to convert to another Rate Period and the Conversion Date. Such notice is to be given, by first class mail, not later than three calendar days after receipt by the Tender Agent of the Conversion Notice. See “Mandatory Tender for Purchase—*Mandatory Tender on Conversion Dates.*”

If less than all of a Sub-Series of the Fiscal 2006 AA Bonds then subject to a particular Rate Mode or Modes are to be converted to a new Rate Mode or Modes, the particular Sub-Series of Fiscal 2006 AA Bonds which are to be converted to a new Rate Mode or Modes shall be selected by the Trustee in such manner as the Trustee deems appropriate subject to the provisions of the Resolutions regarding Authorized Denominations of Fiscal 2006 AA Bonds subject to such Rate Mode.

No Fiscal 2006 AA Bonds may be converted from a Rate Period to a new Rate Period of another duration unless the Trustee and Tender Agent have received an Opinion of Bond Counsel by 10:00 a.m., New York City time, on the Conversion Date.

If the election to convert was withdrawn by the Authority, or if the Remarketing Agent for such Sub-Series has notified the Tender Agent that it has been unable to remarket the Fiscal 2006 AA Bonds on the Conversion Date, the Sub-Series of Fiscal 2006 AA Bonds will bear interest in a Daily Rate Period or, at the option of the Authority and in compliance with the provisions of the Resolution regarding conversion of Rate Modes, any other Rate Period, which Rate Period will be in effect from and after the date on which the Rate Period was to be converted; *provided, however*, unless on or prior to the Conversion Date an Opinion of Bond Counsel is delivered, the Rate Mode for the Sub-Series of Fiscal 2006 AA Bonds not converted shall be the existing Rate Mode.

### **Interest Rates and Reset Dates**

*General.* The rate at which a Sub-Series of the Fiscal 2006 AA Bonds will bear interest during any Rate Period will be the rate of interest that, if borne by the Fiscal 2006 AA Bonds for such Rate Period, in the judgment of the Remarketing Agent for such Sub-Series, having due regard for the prevailing financial market conditions for revenue bonds or other securities the interest on which is excludable from

gross income for federal income tax purposes of the same general nature as the Fiscal 2006 AA Bonds and which are comparable as to credit and maturity or tender dates with the credit and maturity or tender dates of the Fiscal 2006 AA Bonds, would be the lowest interest rate that would enable the Fiscal 2006 AA Bonds to be sold at a price equal to the principal amount thereof, plus accrued interest thereon, if any.

The Fiscal 2006 AA Bonds (other than Purchased Bonds) may not bear interest at a rate greater than nine percent (9%) per annum.

*Daily Rate Period.* The Daily Rate for each Sub-Series for any Business Day is to be determined by the applicable Remarketing Agent for such Sub-Series and announced by 10:00 a.m., New York City time, on such Business Day. For any day which is not a Business Day, the Daily Rate will be the Daily Rate for the immediately preceding Business Day.

If with respect to a Sub-Series (i) a Daily Rate for a Business Day has not been determined by the Remarketing Agent for such Sub-Series, (ii) no Remarketing Agent for such Sub-Series shall be serving under the Resolutions, (iii) the Daily Rate determined by the applicable Remarketing Agent cannot for any reason be in effect for such Business Day or (iv) pursuant to the Remarketing Agreement relating to a Sub-Series the Remarketing Agent is not then required to establish a Daily Rate, the Daily Rate for such Business Day will be the BMA Municipal Index on the date such Daily Rate was to have been determined by the Remarketing Agent for such Sub-Series.

*Weekly Rate Period.* Except as described below, the Weekly Rate is to be determined by the Remarketing Agent for the related Sub-Series and announced by 4:00 p.m., New York City time, on Wednesday of each week or, if Wednesday is not a Business Day, on the next succeeding Business Day. Each Weekly Rate will be in effect for a seven-day period commencing on Thursday and continuing through the next succeeding Wednesday. However, if the Conversion Date upon which a Rate Period has been converted to a Weekly Rate Period is not a Thursday, the initial Weekly Rate will commence on the Conversion Date and will continue through the next succeeding Wednesday which may be less than seven days. The Weekly Rate for such Weekly Rate Period will be determined by the Remarketing Agent for the related Sub-Series and announced by 4:00 p.m., New York City time, on the Business Day before the Conversion Date.

If with respect to a Sub-Series (i) a Weekly Rate has not been determined by the applicable Remarketing Agent for such Sub-Series, (ii) no Remarketing Agent for such Sub-Series shall be serving under the Resolutions, (iii) the Weekly Rate determined by the applicable Remarketing Agent cannot for any reason be in effect or (iv) pursuant to the Remarketing Agreement relating to a Sub-Series the Remarketing Agent is not then required to establish a Weekly Rate, the Weekly Rate will be the BMA Municipal Index on the date such Weekly Rate was to have been determined by the Remarketing Agent.

*Commercial Paper Rate Period.* Except as described below, the Commercial Paper Rate is to be determined by the applicable Remarketing Agent and announced by 1:30 p.m., New York City time, on the first day of each Commercial Paper Rate Period. Unless the Remarketing Agent specifies otherwise, each Commercial Paper Rate Period will be the shorter of (i) seven days, or (ii) the period remaining to and including the final maturity date of the Fiscal 2006 AA Bonds. A Fiscal 2006 AA Bond can have a Commercial Paper Rate Period, and bear interest at a Commercial Paper Rate, different from other Fiscal 2006 AA Bonds in the Commercial Paper Rate Mode.

If with respect to a Sub-Series (i) a Commercial Paper Rate has not been determined by the Remarketing Agent for such Sub-Series, (ii) no Remarketing Agent for such Sub-Series shall be serving under the Resolutions, (iii) the Commercial Paper Rate determined by the applicable Remarketing Agent cannot for any reason be in effect or (iv) pursuant to the Remarketing Agreement relating to a Sub-Series the Remarketing Agent is not then required to establish a Commercial Paper Rate, the Commercial Paper Rate will be the BMA Municipal Index on the date such Commercial Paper Rate was to have been determined by the Remarketing Agent.

*Flexible Rate Period.* Except as described below, the Flexible Rate for any Flexible Rate Period is to be determined by the applicable Remarketing Agent and announced by not later than one (1) day prior

to the Flexible Rate Period and will be in effect from the first day of such Flexible Rate Period through the day prior to the commencement of the next Rate Period. If the applicable Remarketing Agent is unable to remarket all of the Fiscal 2006 AA Bonds of a Sub-Series at the interest rate determined by the Remarketing Agent pursuant to the previous sentence, the Remarketing Agent may at any time prior to the Conversion Date or Reset Date increase the interest rate to that rate which would enable the Fiscal 2006 AA Bonds to be sold on such Conversion Date or Reset Date at a price of par plus accrued interest. No less than twenty (20) Business Days prior to the commencement of each Flexible Rate Period, the Authority shall deliver to the Trustee and the Remarketing Agent written notice of the Authority's determination of the next succeeding Flexible Rate Period, which Flexible Rate Period shall end on a Business Day and shall not be the maturity date of such Fiscal 2006 AA Bonds; provided, however, that if the Authority fails to specify the next succeeding Flexible Rate Period, such Flexible Rate Period shall be the shorter of (i) the same period as the immediately preceding Flexible Rate Period, or (ii) the period remaining to and including the final maturity date of the Fiscal 2006 AA Bonds.

If for any reason the interest rate for the Fiscal 2006 AA Bonds in the Flexible Rate Mode is not or cannot be a Flexible Rate determined by the applicable Remarketing Agent, the Flexible Rate will be equal to Municipal Market Data General Obligation Yield on bonds with the same long term ratings that mature on the same date as the date on which the new Flexible Rate Period for such Fiscal 2006 AA Bonds will end. Such interest rate shall be based upon the Municipal Market Data General Obligation yield for the most recent period for which information is available on the date the interest rate is to be determined. If such index or its equivalent is no longer published, the interest rate on such Fiscal 2006 AA Bonds shall be the interest rate then currently in effect for such Fiscal 2006 AA Bonds.

*Fixed Rate Period.* The Fixed Rate is to be determined by the Authority and the applicable Remarketing Agent or other investment banking firm or firms with which the Authority has entered into an agreement for the purchase, as underwriter, of the Fiscal 2006 AA Bonds on the Conversion Date. If a Fixed Rate has not been determined as aforesaid for any reason, then the Rate Period shall convert to a Daily Rate Mode unless (i) the Authority elects another Rate Mode for such Fiscal 2006 AA Bonds and on or prior to the Conversion Date, an Opinion of Counsel is delivered to the Trustee and the applicable Facility Provider, if any; *provided, however*, unless on or prior to the Conversion Date an Opinion of Bond Counsel is delivered to the Trustee and the Facility Provider, the Rate Mode for the Fiscal 2006 AA Bonds not converted to the Fixed Rate shall be the existing Rate Mode.

*Purchased Bonds.* Purchased Bonds will bear interest at the Purchased Bonds Rate, provided, that such rate shall not exceed twenty five percent (25%) per annum (the "Purchased Bonds Maximum Rate"). If the Purchased Bonds Rate exceeds the Purchased Bonds Maximum Rate, then the Purchased Bonds will bear interest at the Purchased Bonds Maximum Rate, *provided*, that if, thereafter, the Purchased Bonds Rate is less than the Purchased Bonds Maximum Rate, then the Purchased Bonds will continue to bear interest at the Purchased Bonds Maximum Rate until the total interest paid and accrued with respect to such Purchased Bonds is equal to the total interest that the Holder thereof would have received if the Purchased Bonds had borne interest at the Purchased Bonds Rate without the foregoing limitation.

### **Optional Tender for Purchase**

*General.* A Fiscal 2006 AA Bond or any portion thereof equal to an Authorized Denomination may be tendered for purchase, at the Purchase Price, at the option of its registered owner on any Business Day during a Daily Rate Period or a Weekly Rate Period upon giving notice of the registered owner's election to tender in the manner and at the times described below. Notice of an election to tender a Fiscal 2006 AA Bond registered in the name of Cede & Co., as nominee of DTC, is to be given by the DTC Participant on behalf of the Beneficial Owner of the Fiscal 2006 AA Bond and will not be given by DTC.

Notice of the election to tender for purchase a Fiscal 2006 AA Bond registered in any other name is to be given by the registered owner of such Fiscal 2006 AA Bond or its attorney-in-fact.

The notice must state the name of the registered owner or the Beneficial Owner and the principal amount of the Fiscal 2006 AA Bond, the principal amount of the Fiscal 2006 AA Bond to be tendered for purchase and the Business Day on which the Fiscal 2006 AA Bond or portion thereof to be tendered for purchase is to be purchased.



A DTC Participant or the registered owner of a Fiscal 2006 AA Bond must give written notice of its irrevocable election to tender such Fiscal 2006 AA Bond or a portion thereof for purchase at its option to the Tender Agent, at its Delivery Office, and to the applicable Remarketing Agent, in the case of Fiscal 2006 AA Bonds bearing interest in a Daily Rate Mode, by no later than 11:00 a.m. on the Optional Tender Date and in the case of Fiscal 2006 AA Bonds bearing interest in a Weekly Rate Mode by no later than 5:00 p.m., New York City time, on any Business Day which is at least seven (7) days prior to the Business Day on which such Fiscal 2006 AA Bond or portion thereof is to be purchased.

**Mandatory Tender for Purchase**

The Fiscal 2006 AA Bonds are subject to mandatory tender and purchase at the Purchase Price on the following dates (each a “Mandatory Tender Date”):

- (a) on each Conversion Date for Fiscal 2006 AA Bonds being converted to a different Rate Mode;
- (b) on each Reset Date for so long as the Fiscal 2006 AA Bonds bear interest in the Commercial Paper Rate Mode or the Flexible Rate Mode;
- (c) on the last Business Day of the Daily Rate Period, the Weekly Rate Period, the Commercial Paper Rate Mode or Flexible Rate Mode, as the case may be, next preceding the effective date of any expiration or earlier termination of the applicable Credit Facility then in effect, if at least thirty (30) days prior to such termination date such Credit Facility has not been extended or a substitute Credit Facility has not been obtained;
- (d) on the substitution of a Credit Facility, if, solely as a result of such substitution, Moody’s, S&P and Fitch reduce or withdraw the long-term or short-term ratings assigned to any portion of the Fiscal 2006 AA Bonds; and
- (e) on the Business Day immediately preceding the date specified in the Notice of Default delivered by the applicable Facility Provider in accordance with the provisions of the applicable Credit Facility.

**Fiscal 2006 AA Bonds Deemed Purchased**

The Fiscal 2006 AA Bonds or portions thereof required to be purchased upon a tender at the option of the registered owner thereof or upon a mandatory tender will be deemed to have been tendered and purchased for all purposes of the Resolution, irrespective of whether such Fiscal 2006 AA Bonds have been presented and surrendered to the Tender Agent, if on the Tender Date moneys sufficient to pay the Purchase Price thereof are held by the Tender Agent. The former registered owner of a Tendered Bond or a Fiscal 2006 AA Bond deemed to have been tendered and purchased will have no claim thereunder or under the Resolution or otherwise for payment of any amount other than the Purchase Price, and such Fiscal 2006 AA Bond or portion thereof will no longer be Outstanding for purposes of the Resolution.

**Purchase Price and Payment**

The Purchase Price of a Fiscal 2006 AA Bond will be the principal amount of the Fiscal 2006 AA Bond to be tendered, plus accrued and unpaid interest from the immediately preceding Bond Payment Date.

The Purchase Price of a Fiscal 2006 AA Bond held in a book-entry-only system will be paid, in same-day funds, to DTC in accordance with DTC’s standard procedures for effecting same-day payments, as described herein under the heading “BOOK-ENTRY ONLY FORM.” Payment will be made without presentation and surrender of the Fiscal 2006 AA Bonds to the Tender Agent and DTC will be responsible for effecting payment of the Purchase Price to the DTC Participants.

The Purchase Price of any other Fiscal 2006 AA Bonds will be paid, in same-day funds, only after presentation and surrender of the Fiscal 2006 AA Bond to the Tender Agent at its Delivery Office. Payment will be made by 3:00 p.m., New York City time, on the later of the Tender Date or the Business Day on which a Fiscal 2006 AA Bond is presented and surrendered to the Tender Agent.

The Purchase Price is payable solely from, and in the following order of priority, the proceeds of the remarketing of Fiscal 2006 AA Bonds tendered for purchase, moneys made available by the applicable Facility Provider under the applicable Credit Facility and other Available Moneys furnished by or on behalf of the Authority for the purchase of Fiscal 2006 AA Bonds.

### **Remarketing of Fiscal 2006 AA Bonds Upon Tender**

Pursuant to the Remarketing Agreements, the Remarketing Agents are required to use their best efforts to remarket Fiscal 2006 AA Bonds tendered or deemed tendered for purchase. Each Remarketing Agreement sets forth, among other things, certain conditions to the Remarketing Agent's obligations to remarket Fiscal 2006 AA Bonds. If any of the conditions are not satisfied, or if the Remarketing Agent is otherwise unable to remarket any Fiscal 2006 AA Bonds, the Purchase Price of such Fiscal 2006 AA Bonds will be paid from amounts obtained from the Facility Provider under the applicable Credit Facility, if any, as described below, or from any other Available Moneys furnished by or on behalf of the Authority.

On each Tender Date, the Remarketing Agents are to give notice to the Tender Agent specifying the principal amount of Fiscal 2006 AA Bonds which have been tendered for purchase and remarketed. The Tender Agent is, on such Tender Date, to obtain funds under the applicable Credit Facility in accordance with its terms in an amount equal to the difference between the Purchase Price of the Fiscal 2006 AA Bonds subject to purchase and the remarketing proceeds available to the Tender Agent.

### **Standby Purchase Agreements**

The Authority is required to provide a Credit Facility for the benefit of the Owners of the Fiscal 2006 AA Bonds for so long as such Fiscal 2006 AA Bonds bear interest at a Daily Rate, Weekly Rate or Commercial Paper Rate. The Authority is also required to provide a Credit Facility during any Flexible Rate Period if solely as a result of the failure to provide such a Credit Facility, the long-term ratings on the Fiscal 2006 AA Bonds would be reduced by any Rating Agency.

The Authority has entered into a Standby Bond Purchase Agreement with respect to the Fiscal 2006 AA-1 Bonds (the "AA-1 Standby Purchase Agreement") with State Street Bank and Trust Company and California State Teachers' Retirement System (collectively, the "AA-1 Facility Providers"). The Authority has entered into a Standby Bond Purchase Agreement with respect to the Fiscal AA-2 and AA-3 Bonds (the "AA-2 and AA-3 Standby Purchase Agreement" and, together with the AA-1 Standby Purchase Agreement, the "Standby Purchase Agreements") with Dexia Crédit Local, acting through its New York Branch (the "AA-2 and AA-3 Facility Provider" and, together with the AA-1 Facility Providers, the "Facility Providers"). Each of the Standby Purchase Agreements is a Credit Facility as defined in the Resolutions. Each registered owner of a Fiscal 2006 AA Bond will be entitled to the benefits of the Standby Purchase Agreement applicable thereto under which the applicable Facility Provider has agreed to make available to the Tender Agent, upon receipt of an appropriate demand for payment, the Purchase Price for Fiscal 2006 AA Bonds tendered for purchase and not remarketed. The commitments of the Facility Providers under the Standby Purchase Agreements are sufficient to pay a Purchase Price equal to the Outstanding principal of and up to 35 days' interest on the Fiscal 2006 AA Bonds at an assumed interest rate of nine percent (9%) per annum. The commitments of the AA-1 Facility Providers are several but not joint, with each of the AA-1 Facility Providers obligated with respect to 50% of amounts payable by the AA-1 Facility Providers under the AA-1 Standby Purchase Agreement. The scheduled Termination Date of the Credit Facilities is October 27, 2012, in the case of the AA-1 Standby Purchase Agreement, and October 27, 2017, in the case of the AA-2 and AA-3 Standby Purchase Agreement.

Fiscal 2006 AA Bonds, the Purchase Price of which was paid from moneys made available under a Standby Purchase Agreement and not otherwise remarketed, will be registered in the name of the applicable Facility Provider or its nominee ("Purchased Bonds") and all interest accruing thereon from the last date to which interest was paid will accrue for the benefit of, and be payable to, such Facility Provider. The obligation of the Authority to repay amounts advanced by a Facility Provider under a Standby Purchase Agreement to purchase Fiscal 2006 AA Bonds will be evidenced by the Fiscal 2006 AA Bonds purchased by such Facility Provider.

Each Standby Purchase Agreement terminates immediately and without notice upon the occurrence of certain events of default (each a “Termination Event” ). Termination Events include (i) failure of the Authority to pay when due any principal of or premium, if any, or interest on the Fiscal 2006 AA Bonds (regardless of any waiver thereof by the holders of the Fiscal 2006 AA Bonds) or a default by the Authority in the payment of principal of or premium or interest on any other bond, note or other evidence of indebtedness issued, assumed or guaranteed by the Authority (provided, however, that no such failure to pay shall constitute a Termination Event if (A) such failure to pay was caused solely by an error or omission of an administrative or operational nature, (B) funds were available to enable the Authority to make such payment when due and (C) such payment is made within two business days after the Authority’s receipt of written notice of such failure to pay); (ii) the occurrence and continuance of an “Event of Default” under the Second Resolution described under clause (v) of “Summary of the Second Resolution—Defaults and Remedies” in Appendix C hereto, consisting of the Authority’s filing of a petition or otherwise seeking of relief under any federal or State bankruptcy or similar law; (iii) each of Moody’s Investors Service (“Moody’s”), Standard & Poor’s Rating Service (“S&P”) and Fitch Inc. (“Fitch”) shall (x) assign a rating to any debt of the Authority which is secured on a parity with the Fiscal 2006 AA Bonds below “Baa3” in the case of Moody’s and below “BBB-” in the case of S&P and Fitch or (y) withdraw or suspend any such rating for a credit-related reason; (iv) (x) the State or any other governmental authority having jurisdiction over the Authority imposes a debt moratorium, debt restructuring, debt adjustment or comparable restriction on repayment when due and payable of the principal of or interest on any debt obligation of the Authority secured by a lien on Revenues or (y) the Authority (A) applies for or consents to the appointment of, or there shall have occurred the taking or possession by, a receiver, custodian, trustee, liquidator or sequestrator (or other similar official) of itself or of all or of a substantial part of its property or assets, (B) admits in writing its inability, or is generally unable, to pay its debts as they become due, (C) makes a general assignment for the benefit of creditors, (D) files a petition seeking to take advantage of any other law relating to bankruptcy, insolvency, reorganization, liquidation, winding-up or composition or adjustment of debts, or (E) takes any action for the purpose of effecting any of the acts set forth in clauses (A) through (D) above; (v) a final, non appealable judgment shall be issued by a court of competent jurisdiction that the Fiscal 2006 AA Bonds or any other material provision of the Standby Purchase Agreement or the Second Resolution shall cease for any reason to be valid and binding, or the Authority shall initiate legal proceedings or assert in legal proceedings that the Fiscal 2006 AA Bonds or any material provision of the Standby Purchase Agreement or of the Second Resolution is invalid or that the Authority has no liability thereon.

Additionally, each Standby Purchase Agreement provides that the Facility Providers’ respective obligations to purchase Fiscal 2006 AA Bonds shall be suspended immediately and without notice upon the occurrence of certain events (each a “Suspension Event”). Suspension Events include (x) the issuance of a judgment that is appealable or non-final but is otherwise described in the Termination Event set forth in clause (v) above (such judgment a “Nonfinal Invalidity Judgment”) and the passage of 30 days after the issuance thereof during which such Nonfinal Invalidity Judgment has not been overturned or stayed upon appeal (provided that the Facility Providers’ obligations to purchase Fiscal 2006 AA Bonds following the stay of any Nonfinal Invalidity Judgment shall be suspended immediately (without the lapse of another 30 day time period) if such stay is lifted pursuant to a subsequent Nonfinal Invalidity Judgment) and (y) the occurrence of an event described as a Termination Event set forth in clause (i) above, but without regard to the proviso thereof.

Following any Suspension Event described in clause (i), the Facility Providers’ respective obligations to purchase Fiscal 2006 AA Bonds each immediately shall terminate and the Facility Providers shall be under no further obligation to purchase Fiscal 2006 AA Bonds under the applicable Standby Purchase Agreement (i) from the date on which a court of competent jurisdiction shall enter a final, nonappealable judgment that the Fiscal 2006 AA Bonds or any material provision of such Standby Purchase Agreement or of the Second Resolution shall cease for any reason to be valid and binding and (ii) from the date that is three years after the date of issuance of the relevant Nonfinal Invalidity Judgment, if on such date the relevant litigation is still pending and a final and nonappealable judgment related thereto has not been obtained.

Following the occurrence of any Suspension Event, the obligation of the Facility Providers under the applicable Standby Purchase Agreement immediately shall be reinstated and the terms of the applicable Standby Purchase Agreement will continue in full force and effect (unless it shall otherwise have terminated by its terms) as if there had been no such suspension on the date on which (i) in the case of a Suspension Event described in clause (x) above, on the date on which a court of competent jurisdiction shall issue a judgment that the Fiscal 2006 AA Bonds or any material provision of the applicable Standby Purchase Agreement or Second Resolution, as applicable, is valid and binding, and (ii) in the case of a Suspension Event described in clause (y) above, the relevant payment is made (so long as such payment is made within two business days after the Authority's receipt of a written notice of such failure to pay).

Additionally, each Standby Purchase Agreement provides that the Fiscal 2006 AA Bonds are subject to mandatory tender at the option of the applicable Facility Provider upon the occurrence of certain other events of default (each a "Tender Event"). Tender Events include (i) failure of the Authority to pay the fees of the Facility Provider which continues for seven days, (ii) failure by the Authority to observe certain covenants contained in the Standby Purchase Agreements relating to maintenance of the existence of the Authority, (iii) amendment of the Agreement, the Remarketing Agreements, the Resolutions, the Fiscal 2006 AA Bonds or the Lease without the Facility Providers' consent, (iv) failure by the Authority to comply with conversion requirements described in the succeeding paragraph, (v) any representation, warranty, certification or statement made by the Authority (or incorporated by reference) in the Standby Purchase Agreements, the Resolutions, the Agreement, the Fiscal 2006 AA Bonds or the Lease shall prove to have been incorrect in any material respect when made or (vi) the occurrence of certain events of default under the Second Resolution.

Each Standby Purchase Agreement requires the Authority to convert the Fiscal 2006 AA Bonds to a rate other than the Daily Rate, Weekly Rate, Flexible Rate or Commercial Paper Rate on a date not more than six months from the date of receipt by the Authority of a notice from the applicable Facility Provider directing such conversion following the occurrence of certain events (each a "Conversion Event"). Conversion Events include (i) the ratings assigned by Moody's, S&P or Fitch to the Fiscal 2006 AA Bonds are withdrawn or reduced below "A-," "A3" or "A-," respectively, (ii) during any consecutive 12-month period, the product of (A) the principal amount of Purchased Bonds owned by a Facility Provider and (B) the number of calendar days during such 12-month period that such Fiscal 2006 AA Bonds are owned by a Facility Provider exceeds the product of 90 and the average daily amount of the Available Allocated Principal Commitment for such Purchased Bonds during such 12-month period, determined in accordance with such Standby Purchase Agreement, (iii) Purchased Bonds remain outstanding for at least 90 days following the end of the Purchase Period, (iv) the occurrence of a Termination Event or a Tender Event or (v) the Fiscal 2006 AA Bonds shall cease for any reason to be valid, binding and enforceable special obligations of the Authority or the Authority shall initiate legal proceedings or assert in legal proceedings that the Fiscal 2006 AA Bonds are invalid or unenforceable or that the Authority has no liability thereon.

The preceding is a summary of certain provisions expected to be included in the Standby Purchase Agreements and the proceedings under which the Fiscal 2006 AA Bonds are to be issued, and is subject in all respects to the underlying documents, copies of which will be available for inspection during business hours at the office of the Tender Agent. Information regarding the Facility Providers is included herein as "APPENDIX G—DESCRIPTION OF THE FACILITY PROVIDERS." Neither the Authority nor the Underwriters make any representation with respect to the information in "APPENDIX G—DESCRIPTION OF THE FACILITY PROVIDERS."

### **Substitution of a Credit Facility**

The Authority may replace a Credit Facility with a substitute Credit Facility; *provided, however*, that the Sub-Series of the Fiscal 2006 AA Bonds which are secured by such Credit Facility will be subject to mandatory tender, if solely as a result of such replacement, the long-term or short-term ratings assigned to such Fiscal 2006 AA Bonds by Moody's, S&P and Fitch would be reduced or withdrawn. The substitute Credit Facility shall be delivered upon the satisfaction of certain requirements set forth in the Resolutions and the Credit Facility, including but not limited to receipt by the Trustee of: (i) written advice from each of Moody's, S&P and Fitch that upon such substitution the rating assigned thereby to the Fiscal 2006 AA Bonds will not be reduced, suspended or withdrawn as a result of such substitution; (ii) an opinion of

counsel to the new Facility Provider to the effect that such substitute Credit Facility constitutes a legal, valid and binding obligation of such Facility Provider enforceable in accordance with its terms, subject only to bankruptcy, insolvency, moratorium and other laws affecting creditors' rights insofar as the same may be applicable in the event of a bankruptcy, insolvency, moratorium or other similar proceeding or occurrence with respect to such Facility Provider and to equitable principles; (iii) an Opinion of Bond Counsel with respect to the substitution or replacement of the current Credit Facility; and (iv) the written consent of an Authorized Officer of the Authority.

No later than five Business Days prior to the effective date of the substitute Credit Facility the Tender Agent shall give notice to the Holders of the Outstanding Fiscal 2006 AA Bonds, which notice shall contain, among other things: (i) a description of such substitute Credit Facility (including the date of expiration of such Credit Facility); (ii) the name of the Facility Provider of such substitute Credit Facility; (iii) a statement as to the ratings on the Fiscal 2006 AA Bonds as a result of the substitution of such substitute Credit Facility for the then existing Credit Facility; and (iv) a statement that the Opinion of Bond Counsel and the opinion of counsel to the Facility Provider necessary for such substitute Credit Facility to become effective have been obtained. The failure of any Holder of a Fiscal 2006 AA Bond to receive such notice shall not affect the validity of the proceedings in connection with the effectiveness of such substitute Credit Facility.

**Redemption of Fiscal 2006 AA Bonds**

*Optional Redemption—Daily, Commercial Paper or Weekly Rate Periods.* The Fiscal 2006 AA Bonds, while they bear interest at a Daily Rate, Commercial Paper Rate or a Weekly Rate, are subject to redemption prior to maturity at the election or direction of the Authority, on any Bond Payment Date, in whole or in part, at the redemption price of 100% of the principal amount of the Fiscal 2006 AA Bonds to be redeemed, plus accrued interest, if any, to the redemption date.

*Optional Redemption—Flexible Rate Period and Fixed Rate Period.* Unless, at the time the Fiscal 2006 AA Bonds are converted to the Flexible Rate Mode or the Fixed Rate Mode, the Authority establishes other dates and Redemption Prices at which such Fiscal 2006 AA Bonds may be redeemed at the option of the Authority, the Fiscal 2006 AA Bonds in the Flexible Rate Mode or the Fixed Rate Mode shall be subject to redemption prior to maturity at the election of the Authority: (A) in whole or in part on any Reset Date in the case of Fiscal 2006 AA Bonds in the Flexible Rate Mode, at a Redemption Price equal to 100% of the principal amount of each Fiscal 2006 AA Bonds or portion thereof to be redeemed, plus accrued interest, if any, to the day of redemption, or (B) in whole or in part at any time beginning on the tenth anniversary of the Conversion Date, at a Redemption Price of 100% of the principal amount of each Fiscal 2006 AA Bonds or portion thereof to be redeemed plus accrued interest, if any, to the date of redemption.

*Fiscal 2006 AA Bonds—Sinking Fund Redemption.* The Fiscal 2006 AA Bonds are subject to mandatory redemption prior to maturity in part, by lot, in such manner as the Trustee may reasonably determine, at a redemption price of 100% of the principal amount thereof, plus accrued interest to the redemption date, on June 15 in each of the years and in the respective principal amounts, as follows:

<u>Year</u>	<u>Fiscal 2006 AA-1 Bonds Amount</u>	<u>Fiscal 2006 AA-2 Bonds Amount</u>	<u>Fiscal 2006AA-3 Bonds Amount</u>	<u>Total</u>
2028	\$40,000,000	\$20,000,000	\$20,000,000	\$80,000,000
2029	40,000,000	20,000,000	20,000,000	80,000,000
2030	40,000,000	20,000,000	20,000,000	80,000,000
2031	40,000,000	20,000,000	20,000,000	80,000,000
2032†	40,000,000	20,000,000	20,000,000	80,000,000

† Final Maturity

There shall be credited against and in satisfaction of the Sinking Fund Installment payable on any date the principal amount of Fiscal 2006 AA Bonds entitled to such Sinking Fund Installment

(i) purchased with moneys in the Debt Service Fund, (ii) redeemed at the option of the Authority, (iii) purchased by the Authority and delivered to the Trustee for cancellation and (iv) deemed to have been paid in accordance the Second Resolution. Fiscal 2006 AA Bonds purchased with moneys in the Debt Service Fund will be credited toward the next Sinking Fund Installment thereafter to become due. Fiscal 2006 AA Bonds redeemed at the option of the Authority, purchased by the Authority (with moneys other than those on deposit in the Debt Service Fund) or deemed to have been paid in accordance with the Resolution shall be applied in satisfaction, in whole or in part, of one or more Sinking Fund Installments payable on such dates as the Authority shall specify in a written direction of the Authority delivered to the Trustee at least 15 days prior to the earliest date on which notice of redemption of the Fiscal 2006 AA Bonds entitled to such Sinking Fund Installment may be given by the Trustee and the Sinking Fund Installment payable on each date specified in such direction shall be reduced by the principal amount of the Fiscal 2006 AA Bonds so purchased, redeemed or deemed to have been paid in accordance with the Second Resolution to be applied in satisfaction of such Sinking Fund Installment as set forth in such direction.

### **Selection of Bonds to be Redeemed**

In the event less than all of the Outstanding Fiscal 2006 AA Bonds of like maturity are to be redeemed prior to maturity, the Trustee shall select for redemption, using such method of selection as it deems proper in its discretion, the Purchased Bonds of such maturity before selecting any other Fiscal 2006 AA Bonds of such maturity for redemption. Fiscal 2006 AA Bonds of such maturity which are not Purchased Bonds shall be selected by the Trustee in accordance with the provisions of the Second Resolution.

### **Notice of Redemption**

Notice of redemption is to be given by first class mail, postage prepaid, at least 30 days prior to the date fixed for redemption, to the registered owners of Fiscal 2006 AA Bonds to be redeemed at their addresses shown on the books of registry. So long as Cede & Co., as nominee of DTC, is the registered owner of the Fiscal 2006 AA Bonds, notice of redemption is to be sent to DTC. No assurance can be given by the Authority that DTC and DTC participants will promptly transmit notices of redemption to Beneficial Owners.

If, on any redemption date, moneys for the redemption of the Fiscal 2006 AA Bonds to be redeemed, together with interest thereon to the redemption date, are held by the Trustee so as to be available therefor on such date, and if notice of redemption has been mailed, then interest on the Fiscal 2006 AA Bonds to be redeemed will cease to accrue from and after the redemption date and such Fiscal 2006 AA Bonds will no longer be considered to be Outstanding under the Second Resolution.

The notice of redemption may provide that the Fiscal 2006 AA Bonds will be due and payable on the redemption date only if moneys sufficient to accomplish such redemption are held by the Trustee on the scheduled redemption date.

**RATE PERIOD TABLE  
FOR FISCAL 2006 AA BONDS**

	<b>DAILY RATE</b>	<b>WEEKLY RATE</b>	<b>COMMERCIAL PAPER RATE</b>	<b>FLEXIBLE RATE</b>	<b>FIXED RATE</b>
Bond Payment Date	15th day of each calendar month	15th day of each calendar month	If Rate Period is 270 days or less, the next succeeding Reset Date or Conversion Date, and if Rate Period is more than 270 days (i) next succeeding Reset Date or Conversion Date and (ii) 180 days prior to such Reset Date or Conversion Date	June 15th and December 15th	June 15th and December 15th
Record Date	Business Day prior to each Bond Payment Date	Business Day prior to each Bond Payment Date	Business Day prior to each Bond Payment Date	First day of the calendar month during which interest is payable	First day of the calendar month during which interest is payable
Reset Date	Not later than 10:00 a.m. on each Business Day	Not later than 4:00 p.m. on each Wednesday or, if not a Business Day, on the next Business Day	Not later than 12:30 p.m. on the first day of each Commercial Paper Rate Period	Not later than 15 days prior to the first day of the Flexible Rate Period	Conversion Date
Commencement of Rate Period	Reset Date or Conversion Date	Each Thursday	Reset Date or Conversion Date	Conversion Date	Conversion Date
Optional Tender Date	Any Business Day	Any Business Day	Not subject to optional tender	Not subject to optional tender	Not subject to optional tender
Notice Period for Optional Tenders	Written notice not later than 11:00 a.m. on any Business Day	Written notice not later than 5:00 p.m. on any Business Day not less than seven days prior to the Tender Date	Not subject to optional tender	Not subject to optional tender	Not subject to optional tender
Tender Date for Tendered Bonds (optional tender)	Not later than 12:00 p.m. on the Optional Tender Date	Not later than 1:00 p.m. on the Optional Tender Date	Not subject to optional tender	Not subject to optional tender	Not subject to optional tender
Payment Date for Tendered Bonds (optional tender)	Not later than 3:00 p.m. on the Tender Date	Not later than 3:00 p.m. on the Tender Date	Not subject to optional tender	Not subject to optional tender	Not subject to optional tender
Payment Date for Tendered Bonds (mandatory tender)	Not later than 3:00 p.m. on the Tender Date	Not later than 3:00 p.m. on the Tender Date	Not later than 3:00 p.m. on the Tender Date	Not later than 3:00 p.m. on the Tender Date	Not subject to mandatory tender

## SECURITY FOR THE SECOND RESOLUTION BONDS

### Revenues

The Act empowers the Board to establish and collect rates, fees and charges for the use of service provided by the System in order to receive Revenues, which together with other available amounts, will be sufficient to place the System on a self-sustaining basis. All Revenues of the System are deposited by the Board in the Local Water Fund held by the Board. The Authority holds a statutory first lien on the Revenues for the payment of all amounts due to the Authority under the Agreement. In the event that the Board fails to make any required payment to the Authority, the Authority or the Trustee may petition for the appointment, by any court having jurisdiction, of a receiver to administer the affairs of the Board, and, with court approval, establish rates and charges to provide Revenues sufficient to make required payments. However, no holder or owner of any bond or note issued by the Authority, or any receiver of the System, may compel the sale of any part of the System.

The City has covenanted in the Agreement to operate and maintain the System in accordance with the advice and recommendations of the Consulting Engineer. Such obligation to operate and maintain the System may be enforced by the Authority in accordance with the provisions of the Act and the terms of the Agreement and the Lease and is not contingent on payment by the Board. The amounts required to operate and maintain the System are certified to the Board by the City and reviewed by the Consulting Engineer.

Beginning on the first day of each month the Board is required to pay to the Trustee under the First Resolution the Revenues in the Local Water Fund, for deposit in the Revenue Fund established under the First Resolution until the amount so deposited equals the Minimum Monthly Balance and the Required Deposits for such month. The Minimum Monthly Balance is the amount required to accumulate the funds necessary for timely payment of all debt service on Outstanding First Resolution Bonds. Required Deposits are the amounts required to be paid from Revenues for deposit to the Authority Expense Fund (including both periodic and termination payments under Interest Rate Exchange Agreements (see "APPENDIX D—FINANCIAL STATEMENTS—Note 10")), the Debt Service Reserve Fund and the Subordinated Indebtedness Fund, including amounts required for payment of the Second Resolution Bonds and other subordinate debt. See "APPENDIX C—GLOSSARY AND SUMMARY OF CERTAIN DOCUMENTS—Summary of the Agreement—Minimum Monthly Balance."

Amounts on deposit in the Revenue Fund are required to be paid to the following funds established under the First Resolution in the following order of priority: first, to the Debt Service Fund; second, to the Authority Expense Fund; third, to the Debt Service Reserve Fund to replenish any deficiency therein; and fourth, to the Subordinated Indebtedness Fund. If amounts on deposit in such Debt Service Fund or such Debt Service Reserve Fund are less than the requirements thereof, amounts on deposit in the Subordinated Indebtedness Fund are required to be used to make up such deficiency. See "APPENDIX C—GLOSSARY AND SUMMARY OF CERTAIN DOCUMENTS—Summary of the First Resolution—Payments into Certain Funds."

Amounts on deposit in the Subordinated Indebtedness Fund will be available to pay debt service on Second Resolution Bonds. On the first day of each calendar month a portion of the amounts on deposit in the Subordinated Indebtedness Fund will be transferred free and clear of the lien of the First Resolution to the Revenue Fund under the Second Resolution in an amount sufficient, together with the amount on deposit in the Revenue Fund and Debt Service Fund established under the Second Resolution, to make the amount on deposit therein equal the Monthly Balance (as defined in the Second Resolution). The Monthly Balance is the amount required to provide for timely payment of all Debt Service on Outstanding Second Resolution Bonds, Parity Bond Anticipation Notes and Parity Reimbursement Obligations. See "APPENDIX C—GLOSSARY AND SUMMARY OF CERTAIN DOCUMENTS—Definition of Certain Terms Used in Second Resolution—Monthly Balance."

In addition, beginning on the day when no First Resolution Bonds are Outstanding, Revenues are to be deposited from the Local Water Fund into the Revenue Fund established under the Second Resolution. As described below, such Revenues will be used to make payments to the Authority Expense Fund, the Arbitrage Rebate Fund and the Subordinated Indebtedness Fund established under the Second Resolution.



Amounts on deposit in the Revenue Fund established under the Second Resolution are to be paid to the following funds established under the Second Resolution in the following order of priority: first, to the Debt Service Fund; second, if no First Resolution Bonds are then Outstanding, to the Authority Expense Fund; third, to the Debt Service Reserve Fund to replenish any deficiency therein; fourth, to the Arbitrage Rebate Fund; and fifth, if no First Resolution Bonds are then Outstanding, to the Subordinated Indebtedness Fund established under the Second Resolution, the amount required to be deposited in such Fund for such month in accordance with the Authority Budget. See “APPENDIX C—GLOSSARY AND SUMMARY OF CERTAIN DOCUMENTS—Summary of the Second Resolution—Payments into Certain Funds.”

After the Board makes the deposits described above to the First Resolution Revenue Fund in such month from the balance remaining in the Local Water Fund, the Board is required, after paying monthly Board Expenses, to pay the City  $\frac{1}{12}$  of the Operating Expenses for such Fiscal Year. After making such payments, any amounts remaining in the Local Water Fund in each month are paid proportionately (a) to the Trustee for deposit in the First Resolution Revenue Fund until the total of all amounts deposited in the First Resolution Revenue Fund equals the Cash Flow Requirement for such Fiscal Year and (b) to the City until all amounts required to be paid to the City for Operating Expenses for such Fiscal Year have been paid. Pursuant to the Second Resolution, amounts deposited into the First Resolution Revenue Fund in any Fiscal Year in excess of the amounts required to be deposited into the First Resolution’s Debt Service Fund, Authority Expense Fund, Debt Service Reserve Fund, and Arbitrage Rebate Fund are to be deposited into the Subordinated Indebtedness Fund established under the First Resolution until the amount on deposit therein, together with the amounts on deposit in the Revenue Fund and Debt Service Fund established under the Second Resolution, equals the Aggregate Debt Service for such Fiscal Year on Second Resolution Bonds, Parity Bond Anticipation Notes and Parity Reimbursement Obligations. For a more complete description of the required payments from the Local Water Fund, see “APPENDIX C—GLOSSARY AND SUMMARY OF CERTAIN DOCUMENTS—Summary of the First Resolution” and “Summary of the Agreement.”

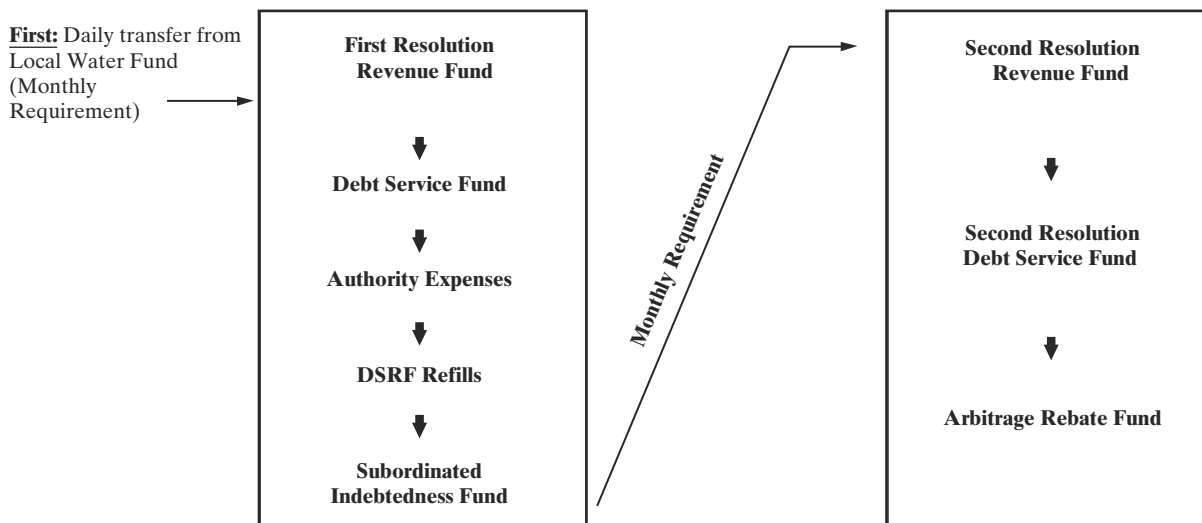
### **Security and Sources of Payment**

The Fiscal 2006 AA Bonds will be on a parity with all other outstanding Second Resolution Bonds heretofore and hereafter issued.

The Fiscal 2006 AA Bonds are payable from and secured by a pledge of (a) amounts on deposit in the Subordinated Indebtedness Fund, subject, however, to the first lien on such amounts in favor of First Resolution Bonds and (b) except as described below under the heading “Debt Service Reserve Fund,” all moneys or securities in any of the funds and accounts established under the Second Resolution, except the Arbitrage Rebate Fund. See “APPENDIX C—GLOSSARY AND SUMMARY OF CERTAIN DOCUMENTS—Summary of the Second Resolution” and “Summary of the Agreement.”

Pursuant to the Agreement, the First Resolution and the Second Resolution, the Revenues received by the Board will be applied in the manner set forth in the following chart. The information contained in such chart is qualified by reference to the Agreement, the First Resolution and the Second Resolution.

# Consolidated Flow of Funds



**Second:** Daily transfer from Local Water Fund (Monthly Requirement) → • Water Board Expenses

**Third:** Daily transfer from Local Water Fund (Monthly Requirement) → • System Operating and Maintenance

**Fourth:** Daily transfer from Local Water Fund (Up to Annual Requirement) → Pro rata to:

- First Resolution Revenue Fund: for annual Debt Service, Authority expenses, DSRF, Subordinate Indebtedness (Second Resolution)
- Systems Operations and Maintenance

**Fifth - Seventh:** Daily transfer from Local Water Fund (After Debt Service is set aside; typically funded during the last few months of the fiscal year) → • City lease payment, operating and maintenance reserve replenishment, surplus including pay as you go capital

## Debt Service Reserve Fund

No deposit will be made to the Debt Service Reserve Fund established under the Second Resolution upon the issuance of the Fiscal 2006 AA Bonds, and the Second Resolution Bonds, Fiscal 2006 AA Bonds will not be secured by any amounts on deposit in such Debt Service Reserve Fund in the future. For a discussion of the Debt Service Reserve Fund established under the Second Resolution, see “APPENDIX C—GLOSSARY AND SUMMARY OF CERTAIN DOCUMENTS—Summary of the Second Resolution—Debt Service Reserve Fund.”

## Rate Covenant

The Board has covenanted in the Agreement to establish, fix, revise and collect rates, fees and charges for the use of, or the services furnished by the System, adequate, together with other available funds, to provide for (i) the timely payment of Principal Installments of and interest on all First Resolution Bonds, and the principal of and interest on any other indebtedness of the Authority (which includes Second Resolution Bonds and other subordinate debt) payable from Revenues, (ii) the proper

operation and maintenance of the System, (iii) all other payments required for the System not otherwise provided for, and (iv) all other payments required pursuant to the Agreement and the Lease.

Without limiting the generality of the foregoing, the Board has covenanted to establish and collect rates, fees and charges sufficient in each Fiscal Year so that Revenues collected in such Fiscal Year will be at least equal to the sum of 115% of Aggregate Debt Service and Projected Debt Service on all First Resolution Bonds (excluding Refundable Principal Installments that are payable from funds held in trust therefor) payable in such Fiscal Year, and 100% of the Operating Expenses and Required Deposits (including debt service on Second Resolution Bonds and other subordinate debt) required to be paid from Revenues for such Fiscal Year (the "Rate Covenant").

The Adjusted Aggregate Debt Service on the Second Resolution Bonds, including the Fiscal 2006 AA Bonds, any Parity Bond Anticipation Notes and Parity Reimbursement Obligations, constitutes Required Deposits within the meaning of the Rate Covenant. The Second Resolution requires that Revenues derived in any Fiscal Year not required to meet any of the payments to be made by the Board during such Fiscal Year be paid by June 30 of such Fiscal Year, for deposit to the Revenue Fund under the First Resolution. Amounts on deposit in the Revenue Fund under the First Resolution on July 1 of a Fiscal Year will reduce the amount of Revenues required to be raised to meet the Required Deposits for such Fiscal Year. A failure to generate Revenues as set forth in this paragraph will not constitute an "event of default" under the Agreement if the Board takes timely action to correct any such deficiency as described in the following paragraph.

Under the First Resolution and the Second Resolution, the Authority is required to submit to the Board by May 1 of each year the Authority Budget for the ensuing Fiscal Year showing the itemized estimated Cash Flow Requirement for such Fiscal Year. The Authority is also required by the Second Resolution to include in its budget and Cash Flow Requirement for each Fiscal Year the Aggregate Debt Service and Projected Debt Service on Second Resolution Bonds. At the beginning of each month, the Authority is to recalculate the Cash Flow Requirement for the then current Fiscal Year and to submit any revisions to the Authority Budget required as a consequence to the Board. The Authority Budget and Cash Flow Requirement are to be used by the Board to set rates, fees and charges.

The Board has covenanted in the Agreement to review the adequacy of rates, fees and charges at least annually. If such annual review, or the report of the Rate Consultant required pursuant to the Agreement, indicates that the rates, fees and charges are or will be insufficient to meet the requirements of the Rate Covenant described above, the Board will promptly take the necessary action to cure or avoid any such deficiency. In addition, under the Agreement, the City, which is responsible for billing, collecting and enforcing collections of rates and charges established by the Board, has agreed that it will diligently pursue all actions necessary to cure or avoid any such deficiency.

The Board has covenanted in the Agreement that it will not furnish or supply or cause to be furnished or supplied any product, use or service of the System free of charge or at a nominal charge, and will enforce (or cause the City to enforce) the payment of any and all amounts owing to the Board for use of the System, except to the extent required by the Act, as in effect on July 24, 1984.

### **Additional Second Resolution Bonds**

The Authority may issue additional Second Resolution Bonds to pay for capital improvements to the System, to pay or provide for the payment of First Resolution Bonds, Second Resolution Bonds, bond anticipation notes, including commercial paper notes, to refund general obligation bonds of the City issued for water or sewer purposes and to fund certain reserves. Under the Second Resolution such additional Second Resolution Bonds may be issued on a parity with all Second Resolution Bonds Outstanding only upon satisfaction of certain requirements including receipt by the Trustee of a certificate by an Authorized Representative of the Authority to the effect that the Revenues for either of the last two Fiscal Years immediately preceding the Fiscal Year in which such Second Resolution Bonds are to be issued were at least equal to the sum of 110% of the Aggregate Debt Service on First Resolution Bonds, Outstanding Second Resolution Bonds, Parity Bond Anticipation Notes and Parity Reimbursement Obligations during such Fiscal Year (excluding from Aggregate Debt Service the amount thereof paid

from a source other than Revenues), and 100% of the sum of the Operating Expenses of the System certified by the City and the Required Deposits for such Fiscal Year (excluding Required Deposits for the payment of Outstanding Second Resolution Bonds, Parity Bond Anticipation Notes and Parity Reimbursement Obligations).

The Authority may issue additional Second Resolution Bonds for the purpose of refunding Outstanding Second Resolution Bonds without satisfaction of the requirements described above only if:

- (a) the average annual debt service on the refunding Second Resolution Bonds does not exceed the average annual debt service on the Second Resolution Bonds to be refunded, and
- (b) the maximum debt service in any Fiscal Year on the refunding Second Resolution Bonds does not exceed the maximum debt service in any Fiscal Year on the Second Resolution Bonds to be refunded.

See “APPENDIX C—GLOSSARY AND SUMMARY OF CERTAIN DOCUMENTS—Summary of the Second Resolution.”

### **Additional Debt on Parity with Second Resolution Bonds**

In addition to other Second Resolution Bonds, the Authority may issue or incur indebtedness which may be secured by a pledge and lien of equal priority as the pledge and lien created by the Second Resolution. The Authority may issue Parity Bond Anticipation Notes, which could include commercial paper notes, and secure the payment of the interest thereon by a pledge of Revenues, which is subordinate to the pledge thereof to secure First Resolution Bonds, of amounts on deposit in the Subordinated Indebtedness Fund established by the First Resolution. The principal of Parity Bond Anticipation Notes may not be secured by a parity pledge or lien.

If, in connection with the issuance of Parity Bond Anticipation Notes or a Series of Second Resolution Bonds, the Authority obtains a Credit Facility or an Interest Rate Exchange Agreement, the Authority’s obligations thereunder may be secured by a pledge of the Revenues and amounts on deposit in the Subordinated Indebtedness Fund established under the First Resolution. The pledge to secure such obligations may be on a parity with the pledge to secure Second Resolution Bonds, except that the Authority’s obligation to reimburse the provider of a Credit Facility for amounts advanced by it to pay the principal of bond anticipation notes may not be secured by a pledge of Revenues and may be secured by the amounts on deposit in the Subordinated Indebtedness Fund only if reimbursement is to be made in substantially equal principal installments payable over not less than eight calendar quarters. If the Authority’s obligations are secured by a parity pledge, they will constitute Parity Reimbursement Obligations.

The Authority’s obligations to pay during a Fiscal Year the interest on Parity Bond Anticipation Notes and Parity Reimbursement Obligations is to be included in the calculation of Debt Service under the Second Resolution for purposes of complying with the financial tests for the issuance of additional Second Resolution Bonds and the computation of the Cash Flow Requirement for such Fiscal Year. See “APPENDIX C—GLOSSARY AND SUMMARY OF CERTAIN DOCUMENTS—Summary of the Second Resolution.”

The Authority is authorized to have outstanding up to \$800 million aggregate principal amount of commercial paper notes (the “Commercial Paper Notes”). The Commercial Paper Notes issued pursuant to the Authority’s existing commercial paper resolutions constitute Parity Bond Anticipation Notes within the meaning of the Second Resolution.

The Commercial Paper Notes are special obligations of the Authority, the proceeds of which are used to pay the costs of capital improvements to the System. The Commercial Paper Notes, Series One, Series Five and Series Six are each secured by standby line of credit agreements which provide liquidity for such Commercial Paper Notes. The Authority’s obligations to the banks providing such standby lines of credit constitute Parity Reimbursement Obligations under the Second Resolution. In March 2003, the Authority authorized its Extendable Municipal Commercial Paper Notes, Series Seven (the “Series Seven Notes”). Principal of and interest on the Series Seven Notes are not secured by any liquidity or credit facility and are payable from remarketing proceeds and the proceeds of additional Series Seven Notes, First Resolution Bonds or Second Resolution Bonds. Interest on the Commercial Paper Notes is secured by the

Revenues of the System and the moneys and investments from time to time on deposit in the Subordinated Indebtedness Fund and the funds and accounts established under the respective commercial paper resolutions authorizing their issuance. However, the pledge of the Revenues and the moneys and investments from time to time on deposit in the Subordinated Indebtedness Fund is subject and subordinate to the pledge thereof made by the First Resolution for the benefit of the holders of First Resolution Bonds.

### **Other Authority Indebtedness**

The Authority has outstanding \$623,625,000 of its Crossover Refunding Bonds that it had previously issued (the “Crossover Bonds”). Each series of Crossover Bonds was issued pursuant to a separate Crossover Refunding Bond Resolution of the Authority. Each series of Crossover Bonds is secured by the proceeds of such series of Crossover Bonds and any investment income thereon, until such Crossover Bonds’ respective tender dates. Guaranteed investment contracts are expected to provide sufficient amounts to pay debt service on the Crossover Bonds until their respective tender dates. The Crossover Bonds have a subordinate lien on the Subordinated Indebtedness Fund under the Second Resolution but have no lien on Revenues. If certain conditions are met on the relevant tender date, the Crossover Bonds of the respective series will be exchanged for First Resolution Bonds to be issued pursuant to the First Resolution and the proceeds of the respective series of Crossover Bonds will be applied to redeem other Outstanding First Resolution Bonds of specified series. The exchanges of its Crossover Bonds for First Resolution Bonds are to occur on June 15, 2006, June 15, 2007 and June 15, 2010 after which there will be no Crossover Bonds outstanding.

### **Derivatives**

In an effort to reduce its borrowing costs over the life of its bonds, the Authority has entered into interest rate exchange agreements. For more information on the Authority’s interest rate exchange agreements, see “APPENDIX D—FINANCIAL STATEMENTS—Note 10”.

### **Covenant of the State**

Section 1045-t of the Act constitutes a pledge of the State to the holders of Authority Bonds not to limit or alter the rights vested in the Authority or the Board by the Act to fulfill the terms of any agreement made with or for the benefit of the holders of the Authority Bonds until such obligations together with the interest thereon are fully met and discharged.

## THE AUTHORITY

### Purpose and Powers

The Authority is a public benefit corporation created pursuant to the Act. Among its powers under the Act, the Authority may borrow money, issue debt and enter into the Agreement, and refund its bonds and notes and general obligation bonds of the City issued for water or sewer purposes. Additionally, the Authority has the power to require that the Board charge and collect sufficient rates to pay the costs of operating and financing the System and to enforce the obligation of the City to adequately operate and maintain the System, regardless of reimbursement by the Board of costs incurred by the City for operation and maintenance.

Pursuant to the Act, there is a statutory first lien on the Revenues in favor of the payment of all amounts due to the Authority under the Agreement. The Revenues remain subject to this lien until provision for payment of all indebtedness issued by the Authority has been made. See “Certain Legal Opinions” for a description of the opinion rendered by Bond Counsel that in the event of a City bankruptcy, a court, exercising reasonable judgment after full consideration of all relevant factors, would not hold that the Revenues are property of the City.

### Membership

The Act authorizes a seven-member board to administer the Authority. Four of the members of the Board of Directors are designated in the Act as *ex officio* members: the Commissioner of Environmental Protection of the City, the Director of Management and Budget of the City, the Commissioner of Finance of the City and the Commissioner of Environmental Conservation of the State. Of the three remaining public members, two are appointed by the Mayor and one is appointed by the Governor. The public members have terms of two years. Pursuant to the Act, all members continue to hold office until their successors are appointed and qualified.

The current members of the Board of Directors are:

<u>Member</u>	<u>Occupation</u>
Mark Page(1).....	Director of Management and Budget of the City
Denise Sheehan(1).....	Acting Commissioner of Environmental Conservation of the State
Martha E. Stark(1).....	Commissioner of Finance of the City
Emily Lloyd(1).....	Commissioner of Environmental Protection of the City
Charles E. Dorkey III(2).....	Partner, Torys
Arthur B. Hill(3).....	Retired, United Parcel Service
Peter J. Kenny(2).....	Retired, Willkie Farr & Gallagher

(1) *Ex officio*.

(2) Appointed by the Mayor.

(3) Appointed by the Governor.

The following is a brief description of certain officers and staff members of the Authority:

Alan L. Anders, Executive Director

Mr. Anders was appointed Executive Director in June 2002 after serving as Treasurer from October 1990. Mr. Anders also serves as Deputy Director for Finance of the Office of Management and Budget of the City. Prior to joining the Authority and the City in September 1990, Mr. Anders had been a senior investment banker for J. P. Morgan Securities since 1977. Prior to that date, he was Executive Director of the Commission on Governmental Efficiency and Economy in Baltimore, Maryland. Mr. Anders is a graduate of the University of Pennsylvania and the University of Maryland Law School.

Marjorie E. Henning, Secretary

Ms. Henning was appointed Secretary in November 1993. Ms. Henning also serves as General Counsel to the Office of Management and Budget of the City. Ms. Henning is a graduate of the State University of New York at Buffalo and the Harvard Law School.

George Zoukee, Treasurer

Mr. Zoukee was appointed Treasurer in September 2005. He is a graduate of Hampshire College in Amherst, Massachusetts and the Boston University Graduate School of Management.

Lawrence R. Glantz, Comptroller

Mr. Glantz was appointed Comptroller in January 2000. He is a graduate of Hofstra University.

Michele Mark Levine, Deputy Comptroller

Ms. Levine was appointed Assistant Comptroller in February 2005. She is a graduate of the State University of New York at Binghamton and the Maxwell School of Citizenship and Public Administration at Syracuse University.

Philip Wasserman, Deputy Treasurer

Mr. Wasserman was appointed Deputy Treasurer in June 2002. He joined the Authority in June of 2000 as a financial analyst and was appointed Assistant Treasurer in November 2000. He is a graduate of Cornell University, Columbia University, and the University of Texas at Austin.

Prescott D. Ulrey, Assistant Secretary

Mr. Ulrey was appointed Assistant Secretary in February 1998. Mr. Ulrey also serves as Counsel to the Office of Management and Budget of the City. He is a graduate of the University of California at Berkeley, the Fletcher School of Law and Diplomacy of Tufts University and Columbia Law School.

Jeffrey M. Werner, Assistant Secretary

Mr. Werner was appointed Assistant Secretary in March 2004. Mr. Werner also serves as Deputy Counsel to the Office of Management and Budget of the City. He is a graduate of Bowdoin College and Columbia Law School.

Raymond Orlando, Manager of Investor Relations

Mr. Orlando was appointed Manager of Investor Relations in June 2000. He is a graduate of the University of Pennsylvania and the John F. Kennedy School of Government at Harvard University.

## THE BOARD

### Purpose and Powers

The Board is a public benefit corporation of the State created by Chapter 515 of the Laws of 1984. The primary responsibility of the Board is to fix, revise, charge, collect and enforce rates and other charges for the System.

The Board is required under the Act to establish rates that will provide adequate funds to pay the debt service on outstanding Authority indebtedness and the City's cost of operating and maintaining the System. In each Fiscal Year, any amounts remaining in the Local Water Fund, after making the required payments under the Agreement, shall be deposited in the General Account in the Operation and Maintenance Reserve Fund and shall be available either as a source of funding for System expenditures or upon certification of the City for deposit to the Authority's Construction Fund to pay for the costs of System capital projects. See "APPENDIX C—GLOSSARY AND SUMMARY OF CERTAIN DOCUMENTS—Summary of the Agreement—Application of Moneys in the Operation and Maintenance Reserve Fund."

Pursuant to the Lease, the Board has a leasehold interest in the System for a term continuing until all Bonds or other obligations issued by the Authority are paid in full or provision for payment has been made. Under the Lease, the City is required to provide billing, collection, enforcement and legal services to the Board. The Board is required to compensate the City for the cost of these services.

### Membership

The Board consists of seven members who are appointed by the Mayor for terms of two years. The Act provides that at least one member will have experience in the science of water resource development and that no member of the Board will be a member of the Authority. The Chairman is appointed by the Mayor. Pursuant to the Act, all members continue to hold office until their successors are appointed and qualified.

The current members of the Board are:

<u>Member</u>	<u>Occupation</u>
James T.B. Tripp, Chair . . . . .	General Counsel, Environmental Defense Fund
Lilyan H. Affinito . . . . .	Retired
Donald Capoccia . . . . .	Principal, BFC Partners, L.P.
Dawn S. Davis . . . . .	Bronx Pro Real Estate Management
Amaziah Howell . . . . .	President, Howell Petroleum Products, Inc.
Stacy Coleman Morse . . . . .	Retired
Maria Santos Valentin . . . . .	Senior Associate General Counsel, Open Society Institute

The following is a brief description of the staff members of the Board:

David B. Tweedy, Executive Director

Mr. Tweedy was appointed Executive Director of the Board in November 2002 and First Deputy Commissioner of DEP in September 2002. For the period from November 2004 to February 2005 he also served as Acting Commissioner. Prior to joining DEP, Mr. Tweedy served for twelve years in various management and executive positions at the New York City Transit Authority ("NYCT"), most recently as Senior Director in the Capital Program Management Department of NYCT, managing non-engineering functions such as Personnel, Systems and Administration and Budgeting. Prior to the NYCT, Mr. Tweedy served as a Vice President at Bankers Trust Company in the Global Operating Services unit. He also worked in financial functions at International Paper Co. Mr. Tweedy is a graduate of Yale University and received an M.B.A. in Finance from Columbia University.

William Kusterbeck, Treasurer

Mr. Kusterbeck has served as Treasurer since his appointment in November 1985. Mr. Kusterbeck has worked for DEP since 1979. He has served in various positions in DEP including



Director of Rates and Revenue, and Director of the Office of Planning. Mr. Kusterbeck is a graduate of Hunter College of the City University of New York and Columbia University Graduate School of Business.

Carmelo Emilio, Deputy Treasurer

Mr. Emilio was appointed Deputy Treasurer in June 2000. He has worked for the City since 1976, and has served as the Chief of Financial Operations at the Water Board from 1996. Prior to joining the Water Board, Mr. Emilio worked with the New York City Office of Management and Budget as a Revenue Analyst. Mr. Emilio is a graduate of Baruch College of the City University of New York.

Albert F. Moncure, Jr., Secretary

Mr. Moncure was named Acting Secretary in February 1997 and Secretary in April 1997. Mr. Moncure also serves as Chief of the Municipal Finance Division of the New York City Law Department. Mr. Moncure has worked for the Law Department since 1986. Mr. Moncure is a graduate of Dartmouth College and the Yale Law School.

## THE DEPARTMENT OF ENVIRONMENTAL PROTECTION

### Organization

Over 5,700 DEP staff members are assigned to the System. Approximately 800 people within the System staff are assigned to the design and construction of ongoing capital projects, including projects within the Capital Improvement Program, as hereinafter defined, and approximately 500 provide administrative and support services to both System and non-System staff. There are approximately 300 additional employees within the DEP staff whose duties are not related to water and sewer service and whose cost is not included as a System cost.

The New York City Department of Design and Construction (the “DDC”) has responsibility for the construction and reconstruction of water and sewer mains in the City. Based upon current workloads, a proportion of DDC’s staff equivalent to 350 full-time positions is devoted to System construction projects.

DEP is managed by a Commissioner, who is appointed by the Mayor. It is organized into seven bureaus: Customer Services; Water and Sewer Operations; Water Supply; Engineering Design and Construction; Wastewater Treatment; Human Resources and Administration; and Executive.

The following are brief descriptions of certain management personnel responsible for the operation of the System.

Emily Lloyd, Commissioner

Ms. Lloyd was appointed Commissioner in February 2005. Prior to joining DEP, Commissioner Lloyd served as Executive Vice President for Columbia University for ten years, most recently as Executive Vice President for Government and Community Affairs and before that as Executive Vice President for Administration. Commissioner Lloyd has devoted much of her professional career to public service. She previously served as Commissioner of the New York City Department of Sanitation, Director of Business Development for the Port Authority of New York and New Jersey and Commissioner for Traffic and Parking for the City of Boston. Ms. Lloyd is a graduate of Wellesley College and received a Master of City Planning from the University of Pennsylvania. She also was a Loeb Fellow at Harvard University, has served on a variety of boards and commissions and is a lifetime Fellow of the National Academy of Public Administration.

David B. Tweedy, First Deputy Commissioner

Mr. Tweedy was appointed First Deputy Commissioner of DEP in September 2002 and Executive Director of the Board in November 2002. For the period from November 2004 to February 2005 he also served as Acting Commissioner. Prior to joining DEP, Mr. Tweedy served for twelve years in various management and executive positions at NYCT, most recently as Senior Director in the Capital Program Management Department of NYCT, managing non-engineering functions such as Personnel, Systems and Administration and Budgeting. Prior to the NYCT, Mr. Tweedy served as a Vice President at Bankers Trust Company in the Global Operating Services unit. He also worked in financial functions at International Paper Co. Mr. Tweedy is a graduate of Yale University and received an M.B.A. in Finance from Columbia University.

Denise M. Richardson, Deputy Commissioner

Denise M. Richardson was appointed Deputy Commissioner for Customer Services in January 2003. Ms. Richardson has held various positions in City government since 1983. Prior to joining Customer Services, Ms. Richardson served as Chief Procurement Officer for the capital construction program of NYCT. Ms. Richardson’s other government positions have included that of Assistant Commissioner/Agency Chief Contracting Officer at the Department of Information Technology and Telecommunications, Deputy Agency Chief Contracting Officer at DEP, Construction Contract Administrator for the Department of General Services (now the Department of Design and Construction), and Director of Administration and Budget Analyst, respectively, at the Department of Sanitation. She also previously worked as Business Manager for Honeywell, Inc. Ms. Richardson is a graduate of Simmons College and received a Master’s Degree in Public Administration/Urban and Regional Planning from Princeton University.

Douglas S. Greeley, P.E., Deputy Commissioner

Mr. Greeley was appointed Director of the Bureau of Water and Sewer Operations in 1996. He has been with DEP since 1973 and has served in numerous capacities, including Chief of System Operations, Chief of the Maintenance Division, and Chief of the Repairs Division of DEP's Bureau of Water Supply and Wastewater Collection. Mr. Greeley is a graduate of the Stevens Institute of Technology. He is a Professional Engineer.

Michael A. Principe, Ph.D., Deputy Commissioner

Dr. Principe was appointed Acting Deputy Commissioner of the Bureau of Water Supply ("BWS") in June 2000 and Deputy Commissioner in May 2001. He has been with DEP since 1981, serving in a variety of roles, most recently as the Deputy Director of BWS and Chief of the Division of Drinking Water Quality Control within BWS. Dr. Principe graduated from Cornell University with a B.S. in Natural Resources, received a M.S. in Environmental Science from SUNY College of Environmental Science and Forestry at Syracuse, New York, and a Ph.D. in Biology from CUNY Graduate School and University Center.

Alfonso R. Lopez, P.E., Deputy Commissioner

Mr. Lopez was appointed Deputy Commissioner of the Bureau of Engineering Design and Construction in August 2005. He has been with the DEP since 1973 and has served in numerous positions including Chief of Process Engineering, Chief of North Facilities Operations, Chief of Biosolids Engineering and Planning Division, Deputy Director of Facilities Operations and most recently as Acting Deputy Commissioner for Wastewater Treatment. Mr. Lopez is a graduate of New York University with a degree in Civil Engineering and is a Professional Engineer.

Dana K. Reed, Deputy Commissioner

Mr. Reed was appointed Deputy Commissioner for Human Resources and Administration in June 2004. He has previously served more than 25 years in the private sector, working in executive level human resources positions at American Telephone & Telegraph, Lucent Technologies and Sara Lee Coffee & Tea. Mr. Reed has also provided consulting services on human resources and management issues. Mr. Reed is a graduate of Southern Illinois University with concentrations in government, psychology and sociology. Mr. Reed has also completed graduate work in the areas of international affairs and business management at the University of Pittsburgh and Pace University, respectively.

Vincent Sapienza, P.E., Acting Deputy Commissioner

Mr. Sapienza was appointed Acting Deputy Commissioner of the Bureau of Wastewater Treatment in September 2005. He has been with DEP since 1983 and has served in numerous positions within the bureau including Chief of Program Development, Chief of Operations Support, Chief of North Facilities Operations, and most recently as Director of Environmental Affairs. Mr. Sapienza is a graduate of Columbia University with a B.S. in Chemical Engineering and has an MBA from Hofstra University. He is a Professional Engineer.

## **Labor Relations**

During the last decade, there have been no strikes or major work stoppages of DEP employees affecting the System. Approximately 95% of DEP's employees are members of labor unions which represent such employees in collective bargaining with the City. The majority of DEP employees who are members of unions are members of District Council 37 of the American Federation of State, County and Municipal Employees ("DC 37"). An agreement with DC 37, covering the period from July 1, 2002 through June 30, 2005, was reached on April 20, 2004 and ratified on June 1, 2004.

## **CAPITAL IMPROVEMENT AND FINANCING PROGRAM**

### **Ten Year Capital Strategy, Current Capital Plan and the Capital Improvement Program**

The City's Ten Year Capital Strategy, which is updated every two years, was published in June 2005 (the "Ten Year Capital Strategy") and includes the projected capital improvements to the System for Fiscal Years 2006 through 2015. The City's Current Capital Plan (the "Current Capital Plan"), which was published in June 2005 and covers Fiscal Years 2006 through 2009, is updated quarterly and is consistent with the Ten Year Capital Strategy for Fiscal Years 2006 through 2009. Funds shown in the first year of the Ten Year Capital Strategy but not committed in that year are generally added to the following year in the Current Capital Plan.

The Ten Year Capital Strategy as modified by the Current Capital Plan comprises the Capital Improvement Program (the "CIP"). The CIP establishes long range programmatic goals for the System and reflects a review of the present condition and long-term needs of the plant and equipment constituting the System. The CIP incorporates the requirements of legal mandates, the present replacement cycle for System facilities, extensions to the present service area, and programs to enhance and optimize the operation of the System. Allowances are included in the CIP for emergency repair and replacement. The value of the actual work done in any given year will differ from that outlined in the CIP. Expected capital commitments for the years beyond the Current Capital Plan will differ from those shown in the CIP due to the addition of new projects, as well as due to changes in project schedules and costs. The capital program projected in the CIP substantially exceeds levels required in order to maintain the current condition of the System.

The CIP was evaluated independently by Metcalf & Eddy. Metcalf & Eddy concluded that the CIP is responsive to the long-term operating requirements of the area served by the System. See "APPENDIX A—LETTER OF METCALF & EDDY, CONSULTING ENGINEERS."

Although Amawalk Consulting, the Authority's rate consultant, has not performed a detailed independent review of the capital program elements and has not made an engineering evaluation of the System, Amawalk Consulting has concluded that the gross level of anticipated commitments through Fiscal Year 2015 as reflected in the CIP appears to be reasonable compared to other large water and wastewater utilities.

The CIP is presented in the following table.

**CAPITAL IMPROVEMENT PROGRAM**

(Thousands of Dollars)

<b>CITY FUNDS</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>Total</b>
<b>WATER SUPPLY AND TRANSMISSION</b>												
Conveyance	\$ 27,190	\$ —	\$ —	\$ —	\$ 50,000	\$ —	\$ —	\$ 301,299	\$ 150,000	\$ 203,455	\$ 300,000	\$ 1,031,944
Kensico—City Tunnel	11,925	—	—	50,000	100,000	100,000	250,000	300,000	200,000	350,000	350,000	1,711,925
City Tunnel No. 3, Stage 1	3,007	84,900	—	—	—	139,000	—	—	—	5,345	5,500	237,752
City Tunnel No. 3, Stage 2	708,825	74,126	5,000	—	—	—	150,000	15,000	—	—	—	952,951
City Tunnel No. 1 Reconstruction	—	25,000	—	—	—	—	—	—	—	—	—	25,000
Miscellaneous Programs	848	—	10,103	—	—	—	—	—	—	—	—	10,951
Subtotal	751,795	184,026	15,103	50,000	150,000	239,000	400,000	616,299	350,000	558,800	655,500	3,970,523
<b>WATER DISTRIBUTION</b>												
Brooklyn—Queens Aquifer	11,940	24,400	34,000	4,000	39,000	4,000	4,000	4,000	4,000	4,000	4,000	137,340
Croton Filtration Project	241,973	193,995	1,016,500	68,000	—	—	—	—	—	—	—	1,520,468
Dam Safety Program	38,846	62,984	8,000	155,875	—	124,000	120,000	55,000	—	—	—	564,705
Trunk Distribution and Main Extension	22,588	65,913	23,684	53,171	41,899	34,446	53,622	28,106	38,298	39,644	41,028	442,399
Trunk Distribution and Main Replacement	121,854	70,518	68,918	68,460	38,107	46,004	73,679	84,634	76,356	78,480	80,813	807,823
Water Quality Preservation	350,727	77,178	736,000	33,300	111,759	20,927	21,255	22,593	11,941	21,600	23,545	1,430,825
Augmentation of Water Supply	—	—	—	—	—	—	—	—	—	—	—	—
Other System Improvements	3,312	2,800	—	—	—	—	—	—	—	—	—	6,112
Subtotal	791,240	497,788	1,887,102	382,806	230,765	229,377	272,556	194,333	130,595	143,724	149,386	4,909,672
<b>WATER POLLUTION CONTROL</b>												
Consent Decree Upgrading & Construction	407,271	315,320	—	142,000	274,000	110,457	8,000	31,000	70,000	28,722	29,554	1,416,324
Plant Upgrading & Reconstruction	108,398	195,842	86,971	214,686	77,150	110,500	95,465	87,489	89,574	73,721	75,932	1,215,728
Sludge Disposal	28,919	7,027	—	—	141,056	—	—	—	—	—	—	177,002
Plant Component Stabilization (1)	248,567	339,943	154,160	325,775	185,936	525,842	330,000	280,000	430,000	236,201	370,633	3,427,057
Water Quality Mandates	(297)	212,182	(13,896)	(17,830)	29,700	104,149	102,500	5,000	7,000	30,000	108,000	566,508
Subtotal	792,858	1,070,314	227,235	664,631	707,842	850,948	535,965	403,489	596,574	368,644	584,119	6,802,619
<b>SEWERS</b>												
Replacement or Augmentation	10,328	30,849	19,130	21,809	27,818	15,000	8,300	5,000	5,000	—	—	143,234
Extensions to Accommodate New Development	82,116	47,218	103,522	76,813	52,509	95,960	122,786	73,641	98,542	107,734	112,047	972,888
Programmatic Response to Regulatory Mandates	—	—	—	9,000	—	—	—	—	—	—	—	9,000
Programmatic Replacement and Reconstruction	715	—	—	—	—	500	—	—	—	—	—	1,215
Replacement of Chronically Failing Components	133,240	99,556	59,327	63,918	42,486	39,268	42,768	40,498	38,500	38,500	38,500	636,561
Trunks	3,837	—	2,568	1,284	—	—	—	—	—	—	—	7,689
Subtotal	230,236	177,623	184,547	172,824	122,813	150,728	173,854	119,139	142,042	146,234	150,547	1,770,587
<b>EQUIPMENT</b>												
Conservation	30,679	24,262	10,000	18,500	10,000	19,000	10,000	10,000	10,000	10,000	10,000	162,441
Management Information Systems	26,101	13,472	2,743	2,224	4,061	2,507	2,670	2,843	3,042	3,246	3,290	66,199
Facility Purchases & Reconstruction	29,266	73,882	31,228	3,975	1,600	38,118	—	—	—	—	—	178,069
Utility Relocation	31,733	25,401	27,725	29,138	39,012	28,175	28,733	28,235	28,310	27,800	27,800	322,062
Vehicles and Equipment	18,312	7,675	7,010	6,950	7,090	7,100	7,050	7,035	7,065	7,085	7,290	89,662
Subtotal	136,091	144,692	78,706	60,787	61,763	94,900	48,453	48,113	48,417	48,131	48,380	818,433
<b>TOTAL CITY FUNDS</b>	<b>2,702,220</b>	<b>2,074,443</b>	<b>2,392,693</b>	<b>1,331,048</b>	<b>1,273,183</b>	<b>1,564,953</b>	<b>1,430,828</b>	<b>1,381,373</b>	<b>1,267,628</b>	<b>1,265,533</b>	<b>1,587,932</b>	<b>18,271,834</b>
<b>STATE, FEDERAL, AND PRIVATE FUNDS</b>												
Water Quality Preservation	2,710	—	—	—	—	—	—	—	—	—	—	2,710
Consent Decree Upgrading & Construction	5,445	—	—	—	—	—	—	—	—	—	—	5,445
Plant Upgrading & Reconstruction	2,563	—	—	—	—	—	—	—	—	—	—	2,563
Plant Component Stabilization (1)	32,129	—	—	—	—	—	—	—	—	—	—	32,129
Water Quality Mandates	25,550	25,000	25,000	25,000	25,000	25,000	25,000	—	—	—	—	175,550
Other System Improvements	3,174	3,024	3,000	3,000	3,000	—	—	—	—	—	—	15,198
<b>TOTAL NON—CITY FUNDS</b>	<b>71,571</b>	<b>28,024</b>	<b>28,000</b>	<b>28,000</b>	<b>28,000</b>	<b>25,000</b>	<b>25,000</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>233,595</b>
<b>TOTAL FUNDS</b>	<b>\$2,773,791</b>	<b>\$2,102,467</b>	<b>\$2,420,693</b>	<b>\$1,359,048</b>	<b>\$1,301,183</b>	<b>\$1,589,953</b>	<b>\$1,455,828</b>	<b>\$1,381,373</b>	<b>\$1,267,628</b>	<b>\$1,265,533</b>	<b>\$1,587,932</b>	<b>\$18,505,429</b>

(1) Plant Component Stabilization includes amounts for the biological nutrient removal program.

Following is a detailed explanation of the major capital program elements within the CIP.

#### *Water Supply and Transmission*

*Kensico-City Tunnel.* The Kensico-City Tunnel will be a 16 mile long tunnel from the Kensico Reservoir to the Van Cortlandt Park Valve Chamber, bypassing the Hillview Reservoir. This tunnel will provide redundancy for the sections of the Catskill and Delaware Aqueducts that run from the Kensico Reservoir to the City.

*Conveyance.* This program will research and develop alternate conveyance conduits and/or water supplies for the City in order to provide more dependability within the Water System. The alternate water supplies could be used during drought situations, to augment the City's daily water supply, or during repairs and inspections of existing aqueducts and tunnels.

*Tunnel 3.* Stages I and II of Tunnel 3 include completion of the Brooklyn/Queens and Manhattan segments. Stage I became operational in July 1998 and has improved the reliability of the transmission system. Stage I amounts also relate to facility improvements at Hillview Reservoir. Completion of the Brooklyn/Queens segment of Stage II will improve services to Staten Island, Brooklyn and Queens. Construction of the Manhattan segment of Stage II will follow completion of the Brooklyn/Queens segment of Stage II which is expected to be completed in 2006. The entire Stage II is scheduled to be completed in 2012. See "THE SYSTEM—The Water System—Water Collection and Distribution."

#### *Water Distribution*

*Croton Filtration Project.* The City is a party to a federal court consent decree with the United States and the State which sets out a timetable for the design and construction of a full-scale water treatment facility to filter Croton System water. See "THE SYSTEM—The Water System—Governmental Regulation."

*Dam Safety Program.* Engineering reports sponsored by the U.S. Army Corps of Engineers indicated that the dams and reservoirs in service in the Catskill, Croton and Delaware Systems are safe but in need of rehabilitation and reconstruction. An ongoing dam reconstruction program has been established for rehabilitation of dams within the Catskill, Croton and Delaware watersheds and the Kenisco Dam.

*Trunk Distribution and Main Extension and Replacement.* This program includes the improvement and extension of the water distribution network for both trunk and distribution water mains. The program facilitates the replacement of undersized or failing system elements, as well as enhancing network reliability.

*Water Quality Preservation.* The City provides for improvements to the upstate watersheds including projects undertaken pursuant to the FADs (as hereinafter defined) in the Catskill and Delaware watersheds such as the acquisition of environmentally sensitive property, the upgrade of non-City owned water pollution control facilities and the construction of an ultraviolet water treatment facility. Other projects in the upstate watersheds include enhanced security systems and repair of the leak in the Rondout-West Branch Tunnel. See "THE SYSTEM—Overview," "THE SYSTEM—The Water System—Water Collection and Distribution," and "THE SYSTEM—The Water System—Governmental Regulation."

#### *Water Pollution Control*

*Consent Decree Upgrading and Construction.* The Clean Water Act (as hereinafter defined) and the State Consent Decrees (as hereinafter defined) require construction of an intercepting sewer for one of the fourteen plants, and the upgrading of six plants. These projects are designed to improve the quality of the surrounding waters.

*Water Quality Mandates.* During periods of heavy rainfall, a combination of stormwater and sewage bypasses treatment and is released into the City's waterways. This program provides for the study, design and construction of the facilities necessary to control the polluting effects of such releases.

*Plant Upgrading and Reconstruction.* This program includes various projects undertaken to upgrade or reconstruct treatment plants, sewage pump stations, motor vessels, regulators and components of the plant treatment system.

*Plant Component Stabilization.* This program includes the replacement and reconstruction of failing components within the fourteen plants and their related facilities necessary to maintain process reliability and the retrofit of five water pollution control plants to decrease the amount of nitrogen discharged into the surrounding water.

#### *Sewers*

*Replacement of Chronically Failing Components.* This program provides for the replacement of sewers that have already collapsed or experience chronic malfunctions (for example, sagging, bends or improper alignment) that cannot be overcome through maintenance or experience chronic malfunction due to inadequate capacity.

*Extensions to Accommodate New Development.* The City must provide acceptable sewage disposal methods for residents within its jurisdiction and must therefore construct new sewers as required. The construction of sewers to replace septic tanks in populated areas avoids health problems associated with viruses, bacteria and other sewage-related pollutants and minimizes stormwater flooding.

#### *Equipment*

*Utility Relocation for Sewers and Water Main Projects.* Under the City's cost-sharing agreement with gas utilities, the City is required to pay 51% of utility work required as a result of water main and sewer construction projects.

### **Historical Capital Program**

The following table presents capital commitments and capital expenditures of the System for Fiscal Years 2000 through 2004. Capital commitments are contractual obligations entered into during the Fiscal Year while capital expenditures represent cash payments made during the Fiscal Year.

**System Capital Commitments and Expenditures**  
(Millions of Dollars)

	FY 2000		FY 2001		FY 2002		FY 2003		FY 2004	
	System Funds(1)	All Funds(2)	System Funds(1)	All Funds(2)	System Funds(1)	All Funds(2)	System Funds(1)	All Funds(2)	System Funds(1)	All Funds(2)
<b>Commitments</b>										
Water Supply and Transmission (3) . . . . .	\$ 71	\$ 71	\$ 130	\$ 130	\$ 135	\$ 135	\$ 63	\$ 63	\$ 39	\$ 39
Water Distribution . . . . .	271	271	178	178	492	492	337	337	480	481
Water Pollution Control	420	420	970	970	806	806	681	687	877	935
Sewers . . . . .	240	240	90	90	199	199	201	202	216	216
Equipment . . . . .	66	66	56	56	37	37	84	84	41	41
Total . . . . .	<u>\$1,068</u>	<u>\$1,068</u>	<u>\$1,423</u>	<u>\$1,423</u>	<u>\$1,669</u>	<u>\$1,669</u>	<u>\$1,366</u>	<u>\$1,373</u>	<u>\$1,653</u>	<u>\$1,711</u>

	FY 2000		FY 2001		FY 2002		FY 2003		FY 2004	
	System Funds(1)	All Funds(2)	System Funds(1)	All Funds(2)	System Funds(1)	All Funds(2)	System Funds(1)	All Funds(2)	System Funds(1)	All Funds(2)
<b>Expenditures</b>										
Water Supply and Transmission (3) . . . . .	\$ 75	\$ 75	\$ 77	\$ 77	\$ 84	\$ 84	\$ 87	\$ 87	\$ 124	\$ 133
Water Distribution . . . . .	168	169	214	215	325	325	269	270	273	371
Water Pollution Control	263	268	275	276	327	328	568	575	742	810
Sewers . . . . .	218	218	196	196	184	185	187	187	221	219
Equipment . . . . .	68	68	78	78	50	50	47	47	44	98
Total . . . . .	<u>\$792</u>	<u>\$798</u>	<u>\$840</u>	<u>\$842</u>	<u>\$970</u>	<u>\$972</u>	<u>\$1,158</u>	<u>\$1,166</u>	<u>\$1,404</u>	<u>\$1,631</u>

Totals may not add due to rounding.

- (1) System Funds include the proceeds of Authority bonds sold directly to the public and those privately placed with the EFC (as defined below) under the revolving fund program and System revenues.
- (2) All Funds include federal and State capital grants.
- (3) Includes capital costs for improvements to upstate water pollution control plants which were paid for with the proceeds of Authority bonds but which are reported as operating expenses in the System's financial statements because such plants are owned by municipalities outside the City.



## **Financing Program**

*Prior Financing.* Since the first issuance of bonds by the Authority in 1985, capital improvements to the System have been financed primarily with (1) proceeds of bonds sold directly to the public and privately placed with EFC in connection with the revolving loan fund program described below, (2) federal and State capital grants, and (3) pay-as-you-go capital paid from System revenues. See “Debt Service Requirements” below.

*Future Financing.* The Authority estimates that approximately 99% of the System’s capital costs will be paid from proceeds of bonds and other forms of indebtedness sold to the public and privately placed with EFC and System revenues. Implementation of the CIP is dependent upon the Authority’s ability to market its securities successfully in the public credit markets. For purposes of forecasting revenue requirements for the System, the principal amount of bonds estimated to be issued for capital purposes as of April 2005, excluding refunding bonds, in each of the Fiscal Years 2006 through 2010 averages approximately \$1.7 billion per year. See the table entitled “Sources and Uses of Capital Funds” below.

Historically, federal grant funds were provided pursuant to the federal Water Pollution Control Act, as amended by the Clean Water Act of 1977 and by the Water Quality Act of 1987 (the “Clean Water Act”), in a program administered by the states, for construction and reconstruction of water pollution control facilities. The City has used these grant funds for five water pollution control plants: Oakwood Beach, Coney Island, Owls Head, Red Hook and North River. The Clean Water Act currently requires states to use federal funds in revolving loan programs in lieu of a federal grant program for water pollution control facilities. To this end, a revolving loan program has been established by the State and administered by EFC in order to use federal financial assistance together with State matching grants in a program to assist municipalities to construct eligible sewage facilities by providing subsidized loans. In addition, pursuant to the Safe Drinking Water Act Amendments of 1996, the State has also initiated a revolving loan program, also administered by EFC, to provide loans for drinking water projects. The Authority has participated in loans under both of the revolving loan programs and anticipates further borrowing under the programs. These revolving loan programs have routinely featured the public sale of bonds by EFC to finance the purchase by EFC of Second Resolution Bonds.

## Sources and Uses of Capital Funds

The following table presents the projected sources and uses of the funds for the System as of April 2005.

<b>Sources and Uses of Capital Funds (Millions of Dollars)</b>							
<b>Description</b>	<b>FY 2005</b>	<b>FY 2006</b>	<b>FY 2007</b>	<b>FY 2008</b>	<b>FY 2009</b>	<b>FY 2010</b>	<b>Period Total</b>
<b>Sources of Funds</b>							
Proceeds from Sale of First Resolution Bonds and Second Resolution Bonds . . .	\$ 2,204.5	\$ 2,122.7	\$ 1,786.9	\$ 1,754.6	\$ 1,717.6	\$ 1,735.0	\$11,321.3
Proceeds from Commercial Paper Notes . . . . .	1,550.9	1,530.0	1,524.6	1,590.0	1,557.0	1,454.0	9,206.5
Total Sources of Funds . . . . .	<u>3,755.4</u>	<u>3,652.7</u>	<u>3,311.5</u>	<u>3,344.6</u>	<u>3,274.6</u>	<u>3,189.0</u>	<u>20,527.8</u>
<b>Uses of Funds</b>							
Refunding of Prior First Resolution Bonds (1) . . . . .	567.9	435.3	105.6	—	—	132.7	1,241.5
Retirement of Commercial Paper Notes . . . . .	1,509.7	1,530.0	1,524.6	1,590.0	1,557.0	1,454.0	9,165.3
Deposit to Construction Fund . . . . .	1,550.9	1,530.0	1,524.6	1,590.0	1,557.0	1,454.0	9,206.5
Other (2) . . . . .	126.9	157.4	156.7	164.6	160.6	148.3	914.5
Total Uses of Funds . . . . .	<u>3,755.4</u>	<u>3,652.7</u>	<u>3,311.5</u>	<u>3,344.6</u>	<u>3,274.6</u>	<u>3,189.0</u>	<u>20,527.8</u>
<b>Construction Fund</b>							
Beginning Balance . . . . .	288.5	427.4	419.4	300.0	300.0	300.0	288.5
Transfer from Proceeds from Commercial Paper Notes . . . . .	1,550.9	1,530.0	1,524.6	1,590.0	1,557.0	1,454.0	9,206.5
Transfer from RPI Trust Fund (3) . . . . .	50.0	50.0	—	—	—	—	100.0
Pay-As-You-Go Capital Construction (4) . . . . .	—	60.0	80.0	100.0	100.0	100.0	440.0
Total Available Construction Funds . . . . .	1,889.4	2,067.4	2,024.0	1,990.0	1,957.0	1,854.0	10,035.0
Less: Total Capital Spending . . . . .	<u>(1,462.0)</u>	<u>(1,648.0)</u>	<u>(1,724.0)</u>	<u>(1,690.0)</u>	<u>(1,657.0)</u>	<u>(1,554.0)</u>	<u>(9,735.0)</u>
Ending Balance . . . . .	<u>\$ 427.4</u>	<u>\$ 419.4</u>	<u>\$ 300.0</u>	<u>\$ 300.0</u>	<u>\$ 300.0</u>	<u>\$ 300.0</u>	<u>\$ 300.0</u>

- (1) For Fiscal Year 2005, includes First Resolution Bonds to be issued to refund RPI Bonds. For Fiscal Year 2006, includes First Resolution Bonds to be issued to refund RPI Bonds and Crossover Bonds. For Fiscal Years 2007 and 2010, includes First Resolution Bonds to be issued to refund Crossover Bonds.
- (2) Includes issuance costs, Debt Service Reserve Fund requirements and capitalized interest.
- (3) Bond proceeds have been deposited in trust to pay the RPI Bonds maturing June 15, 2006.
- (4) Funds projected for Pay-As-You-Go Capital may be used for the defeasance of First Resolution Bonds.

The following table shows projected debt service requirements including payments on outstanding bonds and on future bonds projected to be issued in financing the CIP as of April 2005. As of the date of this Official Statement, the Authority has issued \$524,530,000 First Resolution Bonds and \$229,018,261 Second Resolution Bonds (not including the Fiscal 2006 AA Bonds) in Fiscal Year 2006. As a result of the issuance of the Fiscal 2006 AA Bonds, the Authority currently expects to issue \$400 million less in First Resolution Bonds in Fiscal Year 2006 than reflected in the table below. For additional information, see “—Debt Service Requirements.”

**Projected Future Debt Service Requirements**  
**(Millions of Dollars)**  
**(April 2005)**

<u>Description</u>	<u>Bond Issues(1)</u>	<u>FY 2005</u>	<u>FY 2006</u>	<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>	<u>FY 2010</u>
First Resolution Debt Service							
Outstanding Bonds . . . . .	\$ —	\$ 472.6	\$ 510.9	\$ 500.8	\$525.6	\$ 544.0	\$ 537.9
Anticipated Future First Resolution Bonds							
Fiscal Year 2005 Bonds . . . . .	498.0	0.4	34.8	21.8	21.8	21.8	21.8
Fiscal Year 2006 Bonds . . . . .	<u>1,822.7</u>	—	24.8	109.7	80.7	80.7	80.7
Fiscal Year 2007 Bonds . . . . .	1,486.9	—	—	26.5	117.5	86.4	86.4
Fiscal Year 2008 Bonds . . . . .	1,454.6	—	—	—	29.8	126.6	93.7
Fiscal Year 2009 Bonds . . . . .	1,417.6	—	—	—	—	29.0	123.3
Fiscal Year 2010 Bonds . . . . .	1,435.0	—	—	—	—	—	26.6
Cash defeasance . . . . .	—	—	(19.1)	(17.9)	(52.1)	(47.3)	(19.9)
Total First Resolution Debt Service . . . . .	—	\$ 473.0	\$ 551.4	\$ 640.9	\$723.4	\$ 841.0	\$ 950.5
Subordinated Obligations							
Interest Payments on Commercial Paper Notes . . . . .	—	18.0	34.0	34.0	34.0	34.0	34.0
Outstanding Second Resolution Bonds . . . . .	—	312.7	344.4	349.3	352.1	350.4	353.1
Anticipated Future Second Resolution Bonds							
Fiscal Year 2006 Bonds . . . . .	<u>300.0</u>	—	7.0	29.2	21.7	21.7	21.7
Fiscal Year 2007 Bonds . . . . .	300.0	—	—	7.4	30.8	22.9	22.9
Fiscal Year 2008 Bonds . . . . .	300.0	—	—	—	7.8	31.4	23.5
Fiscal Year 2009 Bonds . . . . .	300.0	—	—	—	—	7.8	31.4
Fiscal Year 2010 Bonds . . . . .	300.0	—	—	—	—	—	7.8
Less: Current Capitalized Interest (2) . . . . .	—	—	—	—	—	—	—
Less: Future Capitalized Interest (3) . . . . .	—	—	—	—	—	—	—
Less: Current EFC Subsidy (4) . . . . .	—	(73.4)	(83.8)	(86.1)	(82.8)	(79.0)	(75.0)
Less: Future EFC Subsidy (5) . . . . .	—	—	(1.9)	(10.1)	(16.8)	(23.2)	(29.7)
Less: EFC Payments (6) . . . . .	—	<u>(8.8)</u>	<u>(7.7)</u>	<u>(6.8)</u>	<u>(5.9)</u>	<u>(4.9)</u>	<u>(3.8)</u>
Actual Debt Service on Subordinated Indebtedness . . . . .	—	\$ 248.4	\$ 292.1	\$ 317.0	\$341.0	\$ 361.0	\$ 385.8
Less: Carryforward Revenues . . . . .	—	<u>(190.0)</u>	<u>(121.2)</u>	<u>(126.0)</u>	<u>(94.2)</u>	<u>(79.9)</u>	<u>(91.0)</u>
Net Debt Service on Subordinated Indebtedness . . . . .	—	\$ 58.4	\$ 171.0	\$ 191.0	\$246.8	\$ 281.1	\$ 294.8
Total Debt Service Payable from Current Revenues (7)	—	<u>\$ 531.5</u>	<u>\$ 722.3</u>	<u>\$ 831.9</u>	<u>\$970.2</u>	<u>\$1,122.2</u>	<u>\$1,245.3</u>

- (1) Includes Crossover Bonds expected to be issued.
- (2) Includes capitalized interest on outstanding Second Resolution Bonds.
- (3) Includes capitalized interest on anticipated future Second Resolution Bonds.
- (4) Includes the estimated EFC subsidy on outstanding Second Resolution Bonds.
- (5) Includes the estimated EFC subsidy on anticipated future Second Resolution Bonds.
- (6) Represents the anticipated transfer of surplus payments used to offset interest payments on Second Resolution Bonds.
- (7) Includes Total First Resolution Debt Service plus Net Debt Service on Subordinated Indebtedness.

Debt service payments on anticipated future bond issues reflect a 30-year term bond structure. The interest rates used in computing the anticipated debt service payments for future fixed rate First Resolution Bonds average 5.75% in Fiscal Year 2005, 6.0% in Fiscal Year 2006, 6.5% in 2007 and 6.75% in each year thereafter. The interest rate used for currently outstanding and future variable rate issues is 3.75% for Fiscal Year 2006 and 4.25% per annum from Fiscal Year 2007 through maturity. The amount of long-term variable rate debt currently outstanding is approximately 11.2% of the Authority's total debt outstanding (not including commercial paper) and is expected to range between 20% and 25% in the future. As shown in the table, debt service payments on anticipated future Second Resolution Bond issues assume that Second Resolution Bonds continue to be issued to EFC and reflect a 30-year term with relatively level annual payments of combined principal and interest. The actual debt service requirements of the Authority will likely differ from the debt service requirements projected in the foregoing table.

The interest rates used in computing the anticipated debt service payments for future EFC bonds secured by Second Resolution Bonds average 5.95% in Fiscal Year 2006, 6.45% in Fiscal Year 2007, and 6.7% in each year thereafter. The Capitalized Interest and EFC subsidy shown in the table include interest capitalized for one year on bonds sold to EFC and subsidies expected to be provided by EFC for these issues, respectively. It is also anticipated that Authority bonds sold to EFC will continue to be structured so that the interest on such bonds is calculated net of the anticipated EFC subsidy.

### **Debt Service Requirements**

The following schedule sets forth the amount required during each Fiscal Year (ending June 30) shown below for the payment of the principal of and the interest (including the Accreted Value of all Capital Appreciation Bonds) on First Resolution Bonds and Second Resolution Bonds assuming that variable rate bonds (including the Fiscal 2006 AA Bonds) bear interest at a rate of 3.75% for Fiscal Year 2006 and 4.25% per annum from Fiscal Year 2007 through maturity. The schedule does not include debt service on any outstanding Commercial Paper Notes.

## Debt Service Requirements

Fiscal Year Ending June 30	Debt Service on Outstanding First Resolution Bonds (1)(2)(3)	Debt Service on Outstanding Second Resolution Bonds (3)(4)	Debt Service on Fiscal 2006 Series AA Bonds			Debt Service on Second Resolution Bonds (3)(4)	Debt Service on First Resolution Bonds and Second Resolution Bonds (1)(2)(3)(4)
			Principal	Interest	Total		
2006	\$ 524,936,824	\$ 258,054,882	\$ —	\$ 9,500,000	\$ 9,500,000	\$ 267,554,882	\$ 792,491,706
2007	525,764,676	262,131,557	—	17,000,000	17,000,000	279,131,557	804,896,234
2008	529,179,990	269,891,213	—	17,000,000	17,000,000	286,891,213	816,071,203
2009	546,136,798	273,180,162	—	17,000,000	17,000,000	290,180,162	836,316,960
2010	562,321,997	281,109,722	—	17,000,000	17,000,000	298,109,722	860,431,720
2011	584,020,157	286,830,474	—	17,000,000	17,000,000	303,830,474	887,850,631
2012	560,328,210	292,009,223	—	17,000,000	17,000,000	309,009,223	869,337,433
2013	556,538,750	253,943,112	—	17,000,000	17,000,000	270,943,112	827,481,862
2014	654,491,302	240,236,234	—	17,000,000	17,000,000	257,236,234	911,727,536
2015	671,841,251	226,682,805	—	17,000,000	17,000,000	243,682,805	915,524,056
2016	662,037,429	227,184,347	—	17,000,000	17,000,000	244,184,347	906,221,775
2017	692,882,072	227,698,198	—	17,000,000	17,000,000	244,698,198	937,580,271
2018	700,854,804	224,565,090	—	17,000,000	17,000,000	241,565,090	942,419,894
2019	701,574,976	222,181,711	—	17,000,000	17,000,000	239,181,711	940,756,687
2020	704,963,616	213,192,005	—	17,000,000	17,000,000	230,192,005	935,155,621
2021	701,954,475	205,073,220	—	17,000,000	17,000,000	222,073,220	924,027,695
2022	702,301,756	202,741,690	—	17,000,000	17,000,000	219,741,690	922,043,446
2023	702,090,869	197,942,385	—	17,000,000	17,000,000	214,942,385	917,033,254
2024	706,957,100	159,644,441	—	17,000,000	17,000,000	176,644,441	883,601,541
2025	705,765,687	157,612,295	—	17,000,000	17,000,000	174,612,295	880,377,983
2026	708,420,110	145,886,514	—	17,000,000	17,000,000	162,886,514	871,306,624
2027	714,039,272	144,550,780	—	17,000,000	17,000,000	161,550,780	875,590,053
2028	652,448,760	134,293,029	80,000,000	17,000,000	97,000,000	231,293,029	883,741,789
2029	632,191,766	126,279,498	80,000,000	13,600,000	93,600,000	219,879,498	852,071,265
2030	655,257,210	112,265,341	80,000,000	10,200,000	90,200,000	202,465,341	857,722,551
2031	696,110,960	107,884,312	80,000,000	6,800,000	86,800,000	194,684,312	890,795,271
2032	707,156,479	81,305,772	80,000,000	3,400,000	83,400,000	164,705,772	871,862,251
2033	686,569,972	61,945,811	—	—	—	61,945,811	748,515,783
2034	663,602,347	36,757,489	—	—	—	36,757,489	700,359,837
2035	663,601,147	8,596,938	—	—	—	8,596,938	672,198,085
2036	491,260,560	—	—	—	—	—	491,260,560
2037	309,796,860	—	—	—	—	—	309,796,860
2038	309,793,110	—	—	—	—	—	309,793,110
2039	511,862,110	—	—	—	—	—	511,862,110
2040	2,213,110	—	—	—	—	—	2,213,110
2041	2,213,110	—	—	—	—	—	2,213,110
2042	2,213,110	—	—	—	—	—	2,213,110
<b>Total</b>	<b>\$21,105,692,734</b>	<b>\$5,641,670,252</b>	<b>\$400,000,000</b>	<b>\$417,500,000</b>	<b>\$817,500,000</b>	<b>\$6,459,170,252</b>	<b>\$27,564,862,986</b>

Totals may not add due to rounding. Debt service is not included for bonds that have been refunded and are no longer Outstanding.

- (1) Assumes that on the respective tender dates, the Crossover Bonds will be exchanged for the First Resolution Bonds and the proceeds of the respective series of Crossover Bonds will be applied to redeem certain Outstanding First Resolution Bonds.
- (2) Assumes that the maturities of Refundable Principal Installments will be amortized as provided in the definition of Adjusted Debt Service rather than paid in full at maturity.
- (3) Net of anticipated subsidy and surplus payments from EFC.
- (4) Net of anticipated capitalized interest from EFC.

## FINANCIAL OPERATIONS

The following tables present certain historical data relating to the System which have been derived from the books and records of the City, the Authority and the Board. For more information, see “INTRODUCTORY STATEMENT—Financial Projection Assumptions.”

### Revenues

The following table presents, on a cash basis, the System revenues received during Fiscal Years 2000 through 2004, as derived from the accounting records utilized in preparation of the statement of cash flows, which is contained in the annual financial statements for Fiscal Years 2000 through 2004.

#### System Revenues (Thousands of Dollars)

<u>Revenue Category</u>	<u>FY 2000</u>	<u>FY 2001</u>	<u>FY 2002</u>	<u>FY 2003</u>	<u>FY 2004</u>
Flat Rate—Water and Sewer Charges(1) . . .	\$ 454,887	\$ 490,181	\$ 513,894	\$ 530,200	\$ 516,655
Metered—Water and Sewer Charges(1) . . .	907,350	872,132	946,922	1,009,677	1,117,797
Meter—Upstate Customers . . . . .	18,994	18,552	21,102	22,790	22,225
Miscellaneous Revenues(2) . . . . .	49,950	53,452	70,482	73,633	77,216
Interest Penalty—Late Charges . . . . .	24,250	24,987	24,930	38,235	41,766
Interest Income . . . . .	74,467	85,724	95,201	97,351	93,567
Tax Lien Sale(3) . . . . .	7,449	40,129	20,152	—	7,783
Total . . . . .	<u>\$1,537,347</u>	<u>\$1,585,157</u>	<u>\$1,692,683</u>	<u>\$1,771,886</u>	<u>\$1,877,009</u>

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- (1) Includes both current payments and payments relating to accounts in arrears.
  - (2) Miscellaneous Revenues are primarily comprised of water and sewer connection and disconnection fees, repair fees, meter installation fees, water usage permits, special meter reading fees and subsidy payments from EFC.
  - (3) In connection with sales of liens on real property securing delinquent property taxes, the City Department of Finance also sold liens on such property securing delinquent water and sewer charges.

The table above records actual cash received by the System and does not reflect either accounts receivable or billing accruals. The System has consistently realized collections of cash revenues in amounts exceeding costs for debt service, current operations and required levels of coverage. This has been achieved while maintaining residential water and sewer service costs at a level which is below the average of comparable large cities.

The forecasted cash flows and anticipated future rate increases take into consideration the anticipated effects of new initiatives by the Board and DEP to enhance the efficiency of collection for current water and sewer billings. It is assumed that some of these initiatives or others will gradually result in a 1% per Fiscal Year increase in the overall rate of cash collections for frontage customers over the next two Fiscal Years and a 1% increase per Fiscal Year of cash collections for metered customers over the next four Fiscal Years, in addition to increases from higher rates. An additional \$50 million in non-recurring revenue is also assumed in each Fiscal Year during the forecast period to account for the expected collection of a portion of the outstanding accounts receivable balance. In the event that DEP is not as successful as anticipated in implementing the enhancement to current collection strategies, the actual increases in user rates in future Fiscal Years may be higher than the increases currently forecasted. For a more detailed discussion of billing and collection, including collection initiatives, see “RATES AND BILLINGS.”

**Expenses**

The following table presents System expenses for Fiscal Years 2000 through 2004 on an accrual basis which have been derived from the accounting records utilized in preparation of the annual financial statements for Fiscal Years 2000 through 2004. These expenses represent operation, maintenance and general expenses excluding the lease rental payment to the City, bad debt expense and capital costs for improvements to upstate water pollution control plants that were paid for with the proceeds of Authority bonds but that are reported as operating expenses in the System's financial statements because such plants are owned by municipalities outside the City.

**System Expenses  
(Thousands of Dollars)**

<u>Expense Category</u>	<u>FY 2000</u>	<u>FY 2001</u>	<u>FY 2002</u>	<u>FY 2003</u>	<u>FY 2004</u>
Water Operations(1)					
Personal Service(2) .....	\$118,598	\$120,797	\$129,292	\$135,627	\$141,927
Other Than Personal Service(3) .....	<u>146,331</u>	<u>165,068</u>	<u>181,034</u>	<u>176,913</u>	<u>171,821</u>
Total Water Operations .....	264,929	285,865	310,326	312,540	313,748
Wastewater Operations(1)					
Personal Service(2) .....	187,003	188,704	197,522	196,851	199,568
Other Than Personal Service(3) .....	<u>158,037</u>	<u>169,459</u>	<u>169,548</u>	<u>183,200</u>	<u>190,269</u>
Total Wastewater Operations .....	<u>345,040</u>	<u>358,163</u>	<u>367,070</u>	<u>380,051</u>	<u>389,837</u>
Administrative and General(4) .....	10,092	11,215	14,171	15,181	19,853
Indirect Expenses(5) .....	<u>40,811</u>	<u>41,195</u>	<u>53,361</u>	<u>51,613</u>	<u>70,217</u>
Total System .....	<u>\$660,872</u>	<u>\$696,438</u>	<u>\$744,928</u>	<u>\$759,385</u>	<u>\$793,655</u>

- 
- (1) Certain historical, administrative and overhead costs of DEP were allocated to the water and sewer functions based upon the proportion of applicable personnel within DEP.
  - (2) Personal Service costs include salaries, fringe benefits and pension costs.
  - (3) Other Than Personal Service costs include real estate taxes paid to upstate communities for watershed properties, land-based sludge disposal costs and for electricity, chemicals and supply costs.
  - (4) Administrative and General costs include Authority and Board expenses, excluding Authority expenses for the defeasance of debt.
  - (5) Indirect Expenses include City agency support, customer accounting, and judgments and claims costs.

## Projected Revenues

As indicated in the table below, user payments are projected as of April 2005 to increase from approximately \$1.7 billion in Fiscal Year 2005 to approximately \$2.5 billion in Fiscal Year 2010. Projected rate increases in future Fiscal Years provide the majority of the increase in user payments. Upstate revenues are projected to increase from approximately \$24.1 million in Fiscal Year 2005 to approximately \$35.5 million in Fiscal Year 2010. This revenue growth is due to expected increases in the cost of water supply services. Miscellaneous revenues include fees from activities such as the review, inspection, and approval of System connections. The projected revenues assume water consumption will decline by 0.5% each Fiscal Year over the forecast period.

### Projected Revenues (Millions of Dollars)

<u>Description</u>	<u>FY 2005</u>	<u>FY 2006</u>	<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>	<u>FY 2010</u>
Operating Revenues						
User Payments (1) . . . . .	\$1,665.5	\$1,882.9	\$1,949.1	\$2,095.6	\$2,283.3	\$2,466.6
Upstate Revenues . . . . .	24.1	26.3	28.5	31.0	33.3	35.5
Subtotal Service Revenue . . . . .	1,689.5	1,909.2	1,977.6	2,126.6	2,316.6	2,502.1
Miscellaneous Revenues . . . . .	5.8	6.1	6.4	6.8	7.1	7.4
Subtotal Operating Revenue . . . . .	1,695.4	1,915.3	1,984.0	2,133.3	2,323.7	2,509.5
Nonoperating Revenues						
Interest Income on System Funds (2) . . . . .	50.7	65.3	75.7	84.6	94.2	102.4
Total Revenues . . . . .	<u>\$1,746.1</u>	<u>\$1,980.6</u>	<u>\$2,059.7</u>	<u>\$2,217.9</u>	<u>\$2,417.9</u>	<u>2,611.9</u>

Figures are calculated on a cash basis.

Totals may not add due to rounding.

Source: Amawalk Consulting.

- (1) Includes late payment charges.
- (2) Includes interest income on the Construction Fund, Debt Service Fund and the Debt Service Reserve Fund. Interest earnings do not take into account the reduction in Debt Service Fund deposits that will result from the projected defeasance of Bonds.



## Projected Operating and Maintenance Expenses

The table set forth below shows, for Fiscal Years 2005 through 2010, the System's projected operation and maintenance expenses as of April 2005.

### Projected Operation and Maintenance Expense (Millions of Dollars)

<u>Line No.</u>	<u>Description</u>	<u>FY 2005</u>	<u>FY 2006</u>	<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>	<u>FY2010</u>
1	Authority/Board Operations . . . . .	\$ 19.4	\$ 29.0	\$ 32.7	\$ 28.4	\$ 29.7	\$ 31.1
2	Net Authority Expense for the Defeasance of Debt . .	150.0	60.0	0.0	0.0	0.0	0.0
Water Operations							
3	Personal Services . . . . .	144.2	145.9	149.4	153.0	159.0	162.8
4	Other Than Personal Services . . . . .	211.9	230.1	236.8	243.9	265.5	273.5
5	Total Water Operations. . . . .	356.1	376.0	386.2	396.9	424.5	436.4
Wastewater Operations							
6	Personal Services . . . . .	227.1	230.9	236.4	242.0	247.8	253.7
7	Other Than Personal Services . . . . .	213.7	227.8	232.8	239.1	245.7	252.5
8	Total Wastewater Operations . . . . .	440.9	458.7	469.2	481.2	493.5	506.2
9	Indirect Expenses . . . . .	12.9	12.9	12.9	12.9	12.9	12.9
10	Judgments and Claims . . . . .	8.0	8.0	8.0	8.0	8.0	8.0
11	Total Operating Expenses . . . . .	987.3	944.6	908.9	927.3	968.7	994.6
12	Less: Trust Account Withdrawals . . . . .	0.0	0.0	0.0	(20.0)	(45.0)	(30.1)
13	Net Operating Expenses . . . . .	987.3	944.6	908.9	907.3	923.7	964.5
14	Less: Credit for Prior Year Excess O&M Payment .	(3.3)	0.0	0.0	0.0	0.0	0.0
15	Net Operating Expense Payments . . . . .	<u>\$983.9</u>	<u>\$944.6</u>	<u>\$908.9</u>	<u>\$907.3</u>	<u>\$923.7</u>	<u>\$964.5</u>

Totals may not add due to rounding.  
 Figures are calculated on a cash basis.  
 Source: Amawalk Consulting.

Operation and Maintenance Expenses include administrative costs associated with the Authority and the Board, direct operating costs for the System, indirect operating costs of DEP, and other expenses and adjustments to annual operating expenses. Each of these is explained more fully below.

*The Authority/Board Operations.* Administrative expenses of the Authority and the Board, shown on Line 1 of the table above, include annual fees required by EFC in connection with the Authority's participation in the State Revolving Fund Program. These fees are projected to be \$8.8 million in Fiscal Year 2005 and \$10 million in Fiscal Year 2006 and are expected to increase as the outstanding principal of bonds issued to EFC increases. Other expenses of the Authority include but are not limited to payments under interest rate exchange agreements, fees related to adjustable rate bonds and commercial paper notes and the management of investments. Net receipts received under interest rate exchange agreements are netted against Authority expenses.

*Water Operations.* The operating costs of the Water System include direct operation and maintenance costs applicable to one or more functional areas of the Water System and the distribution system as well as certain indirect operating costs of the DEP which are allocated between the Water System and the Sewer System. The operating costs of the Water System are divided into personal services costs and other than personal services costs. Personal services costs include direct salary costs plus fringe benefit and pension costs.

Other than personal services costs include property taxes paid to upstate communities for watershed properties as well as chemicals, electricity, and other expenses.

All but a small percentage of the Water System functions by gravity so that electricity costs necessary to maintain normal water transmission and distribution are relatively small. In drought conditions, additional pumping is necessary for optimal distribution of water available from the System, thereby causing increased electricity costs.

Personal services costs assume a 2.5% increase per year from Fiscal Years 2005 through 2010. Other than personal services costs are assumed to increase at an estimated rate of 3% per year for the forecast period.

In accordance with the watershed protection agreement, DEP will implement additional programs which will enhance the ability of the City and the communities located in the watershed area to protect the quality of the water supply. Such programs will include certain capital investments which are contained within the CIP. The forecasted operation and maintenance expenses for the Water System reflect the expected increase in operation and maintenance costs due to the Watershed Agreement.

The forecast also includes an increase in operation and maintenance expenses for the ultraviolet treatment facility, beginning in Fiscal Year 2009.

*Wastewater Operations.* The operating costs of the Sewer System include direct operation and maintenance costs applicable to one or more functional areas of the Sewer System as well as certain indirect operating costs of DEP allocated to the Water System and the Sewer System. The operating costs of the Sewer System are also divided into personal services and other than personal services costs. Personal services costs include direct salary costs plus fringe benefits and pension costs.

Other than personal services costs include electricity for the water pollution control plants, pump stations and service yards, chemicals, and other expenses. Electricity, which represents a significant expense in operating the treatment plants and pump stations, is supplied primarily by the Power Authority of the State of New York. A major component of other than personal services cost is biosolids management. The annual costs of biosolids management are anticipated to remain relatively constant at approximately \$50 million per year for the next several years in accordance with the terms of current re-use contracts. Certain other cost adjustments are reflected in the forecasted cash flow as adjustments are made to specific operating programs based upon System needs.

*Other Expenses.* Other expenses of the System include indirect expenses and judgments and claims. Indirect expenses, shown on Line 9 of the table, reflect costs allocated to the System for support provided by various City agencies and departments. Services provided include budget preparation and review, cost and revenue accounting, billing and collection, and legal support. The method of allocating these costs to the System is based upon costs initially allocated to DEP and subsequently divided between those attributable to water and sewer and those costs associated with other activities of DEP. The costs allocated to DEP as a whole are derived from the total costs of City support agencies and departments and a formalized cost allocation plan which distributes the costs to affected departments and agencies. DEP's billing and collection expenses are included in the operation and maintenance costs of the Water System and the Wastewater System.

*Credits Against Operation and Maintenance Expense.* Pursuant to a consent decree (the "1989 Consent Decree") entered into in 1989 under the Marine Protection Research and Sanctuaries Act of 1972 ("MPRSA"), as amended by the Ocean Dumping Ban Act of 1988 (the "Ban Act"), DEP ceased the ocean disposal of sludge in June 1992. The Ban Act and the 1989 Consent Decree provide that 85% of the fees and penalties paid shall be deposited into a trust account and shall be available to reimburse the City for costs incurred for developing alternative biosolids management facilities. As of January 31, 2005, the value of the trust account was \$87.1 million. It is assumed that this value will increase with interest earnings at the rate of 2% per annum, until withdrawals are made. A portion of the balance of the fees and penalties was paid to United States Environmental Protection Agency ("USEPA") with the remainder divided equally between the New York State Water Pollution Control Revolving Fund and the New York State Clean Oceans Fund. It is anticipated that \$20 million in Fiscal Year 2008, \$45 million in Fiscal Year 2009, and \$30.1 million in Fiscal Year 2010 will be available as an offset to operation and maintenance expenses.

## Projected Financial Operations

The following table shows a summary of the forecasted cash flows for the Authority as of April 2005 for Fiscal Year 2005 through Fiscal Year 2010. See “CAPITAL IMPROVEMENT AND FINANCING PROGRAM—Debt Service Requirements.” The projected rate increases described herein under “RATES AND BILLING—Rates” have been assumed in order to meet cash expenditure requirements to comply with debt service requirements pursuant to the First Resolution and the Second Resolution. See “FINANCIAL OPERATIONS—Projected Revenues.” As shown on Line 30 of the table, positive net surpluses are projected to be maintained throughout the reporting period. Line 31 illustrates the coverage of First Resolution debt service by current revenues available for debt service. Line 32 illustrates the coverage of First Resolution and Second Resolution debt service by current revenues available for debt service.

### Forecasted Cash Flows (Millions of Dollars)

Line No.	Description	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010
	<b>Operating Revenues</b>						
1	Water and Sewer User Payments . . . . .	\$1,665.5	\$1,882.9	\$1,949.1	\$2,095.6	\$2,283.3	\$2,466.6
2	Upstate Revenue . . . . .	24.1	26.3	28.5	31.0	33.3	35.5
3	Miscellaneous Revenue . . . . .	5.8	6.1	6.4	6.8	7.1	7.4
	<b>Other Revenues</b>						
4	Interest on Funds . . . . .	50.7	65.3	75.7	84.6	94.2	102.4
5	<b>Current Revenues Available for Debt Service . . . . .</b>	<u>1,746.1</u>	<u>1,980.6</u>	<u>2,059.7</u>	<u>2,217.9</u>	<u>2,417.9</u>	<u>2,611.9</u>
	<b>First Resolution Debt Service</b>						
6	Outstanding Bonds . . . . .	472.6	510.9	500.8	525.6	544.0	537.9
7	Anticipated Future First Resolution Bonds . . . . .	0.4	40.5	140.1	197.8	297.0	412.6
8	<b>Total First Resolution Debt Service . . . . .</b>	<u>473.0</u>	<u>551.4</u>	<u>640.9</u>	<u>723.4</u>	<u>841.0</u>	<u>950.5</u>
	<b>Subordinated Obligations</b>						
9	Interest Payments on Commercial Paper						
	Notes . . . . .	18.0	34.0	34.0	34.0	34.0	34.0
10	Outstanding Second Resolution Bonds . . . . .	312.7	344.4	349.3	352.1	350.4	353.1
11	Anticipated Future Second Resolution						
	Bonds . . . . .	—	7.0	36.6	60.3	83.7	107.2
12	Less: EFC Subsidy . . . . .	(82.2)	(93.3)	(103.0)	(105.5)	(107.1)	(108.5)
13	<b>Actual Debt Service on Subordinated</b>						
	Indebtedness . . . . .	248.4	292.1	317.0	341.0	361.0	385.8
14	Less: Carryforward Revenues . . . . .	(190.0)	(121.2)	(126.0)	(94.2)	(79.9)	(91.0)
15	<b>Net Debt Service on Subordinated</b>						
	Indebtedness . . . . .	58.4	171.0	191.0	246.8	281.1	294.8
16	<b>Total Debt Service Payable from Current Revenues (line 8 + line 15) . . . . .</b>	<u>531.5</u>	<u>722.3</u>	<u>831.9</u>	<u>970.2</u>	<u>1,122.2</u>	<u>1,245.3</u>
	<b>Operating Expenses</b>						
17	Authority/Board Operations . . . . .	19.4	29.0	32.7	28.4	29.7	31.1
18	Net Authority Expense for the Defeasance of Debt . . . . .	150.0	60.0	—	—	—	—
19	Water System . . . . .	356.1	376.0	386.2	396.9	424.5	436.4
20	Wastewater System . . . . .	440.9	458.7	469.2	481.2	493.5	506.2
21	Indirect Expense . . . . .	12.9	12.9	12.9	12.9	12.9	12.9
22	Judgments and Claims . . . . .	8.0	8.0	8.0	8.0	8.0	8.0
23	<b>Total Operating Expenses . . . . .</b>	<u>987.3</u>	<u>944.6</u>	<u>908.9</u>	<u>927.3</u>	<u>968.7</u>	<u>994.6</u>
24	Less: Trust Account Withdrawals . . . . .	—	—	—	(20.0)	(45.0)	(30.1)
25	<b>Net Operating Expenses . . . . .</b>	<u>987.3</u>	<u>944.6</u>	<u>908.9</u>	<u>907.3</u>	<u>923.7</u>	<u>964.5</u>
26	Less: Credit for Prior Year Excess O&M Payment . . . . .	(3.3)	—	—	—	—	—
27	Rental Payment to the City of New York . . . . .	109.5	127.7	144.7	160.5	181.0	201.0
28	Pay-As-You-Go Capital Construction . . . . .	—	60.0	80.0	100.0	100.0	100.0
29	<b>Total Expenses . . . . .</b>	<u>1,093.5</u>	<u>1,132.3</u>	<u>1,133.6</u>	<u>1,167.9</u>	<u>1,204.7</u>	<u>1,265.5</u>
30	<b>Net Surplus (line 5-line 16-line 29) . . . . .</b>	<u>\$ 121.2</u>	<u>\$ 126.0</u>	<u>\$ 94.2</u>	<u>\$ 79.9</u>	<u>\$ 91.0</u>	<u>\$ 101.1</u>
31	<b>First Resolution Debt Service Coverage (line 5/line 8) . . . . .</b>	3.69x	3.59x	3.21x	3.07x	2.87x	2.75x
32	<b>First and Second Resolution Debt Service Coverage (line 5/line 16) . . . . .</b>	3.29x	2.74x	2.48x	2.29x	2.15x	2.10x

Source: Amawalk Consulting.

Column subtotals and totals may reflect adjustments for rounding of amounts shown in individual line items.

## RATES AND BILLINGS

### Rates

The Board is responsible for setting rates in compliance with the Rate Covenant. See “SECURITY FOR THE BONDS—Rate Covenant.” The Board retains the firm of Amawalk Consulting for the purpose of conducting a detailed review of the structure of water and sewer rates. The Board considers the results of Amawalk Consulting rate studies in establishing its rates and charges for service.

The System’s rates and charges are largely exempt from federal and State regulation. Water rates, fees and charges for water supply are the responsibility of the Board and are not subject to further approval or regulation except for rates for upstate users. Currently approximately 1% of System Revenues are collected from such upstate users. Sewer charges are established by the Board as a percentage of water charges. Participation in the Construction Grants Program, however, requires the maintenance of sewer charges sufficient to defray costs of operation, maintenance and replacement. The Board, as a matter of policy, conforms with these requirements when setting sewer charges. The Board uses data compiled from meter readings for billings and to determine the effectiveness of City-mandated conservation measures.

The following table sets forth the changes in rates for water and sewer service since 1986:

### History of Water and Sewer Rate Increases

Effective Date	Change in Flat-Rate Water	Change in Metered Water	Metered Water Rate (per ccf)(1)	Change in Sewer
July 1, 1986	Increased 9.9%	Increased 9.9%	72.5¢	Remained at 60% of watercharge
July 1, 1987	Increased 12%	Increased 12%	81¢	Increased to 70% of watercharge
July 1, 1988	Increased from \$14.06 to \$26.40 per year for each additional family above the single family assumed in an individual flat-rate account.	No change	81¢	Increased to 75% of watercharge
July 1, 1989	Increased from \$26.40 to \$41.86 per year for each additional family above the single family assumed in an individual flat-rate account. Remaining flat-rate charges increased by 7.8%.	Increased 7.8%	87¢	Increased to 88% of watercharge
Jan. 1, 1990	Increased 9%	Increased 9%	95¢	Increased to 112% of watercharge
July 1, 1991	Increased 6.4%	Increased 6.4%	\$1.01	Increased to 136% of watercharge
July 1, 1992	No change	No change	\$1.01	Increased to 159% of watercharge
July 1, 1993	No change	No change	\$1.01	No change
July 1, 1994	No change	No change	\$1.01	No change
July 1, 1995	Increased 5%	Increased 5%	\$1.06	No change
July 1, 1996	Increased 6.5%	Increased 6.5%	\$1.13	No change
July 1, 1997	Increased 6.5%	Increased 6.5%	\$1.20	No change
July 1, 1998	Increased 4%	Increased 4%	\$1.25	No change
July 1, 1999	Increased 4%	Increased 4%	\$1.30	No change
July 1, 2000	Increased 1%	Increased 1%	\$1.31	No change
July 1, 2001	Increased 3%	Increased 3%	\$1.35	No change
July 1, 2002	Increased 6.5%	Increased 6.5%	\$1.44	No change
July 1, 2003	Increased 5.5%	Increased 5.5%	\$1.52	No change
July 1, 2004	Increased 5.5%	Increased 5.5%	\$1.60	No change
July 1, 2005	Increased 3%	Increased 3%	\$1.65	No change

(1) ccf: 100 cubic feet.

*Projected Rates.* Although the Board sets rates for an annual period, it may increase rates during such period, as required. As of April 2005, forecasted debt service, operating and other costs for the System indicated that the anticipated future rate increases to be set by the Board for water and sewer services combined were 3% per year in Fiscal Year 2006, 5.6% per year in Fiscal Year 2007 and 8.7% per year in Fiscal Year 2008 through Fiscal Year 2010. Prior to setting rates for an annual period, the Board publicly notices a rate increase and conducts public hearings on that rate increase. In June 2005, the 3% increase for Fiscal Year 2006 was approved.

*Basic Sewer Charge.* For all properties connected to the Sewer System, or legally required to be connected after receiving proper notice, there is a charge imposed equal to a fixed percentage of the property’s water charge. Since July 1, 1992, the sewer charge has remained at 159% of the water charge.

*Sewer Allowances.* Certain commercial customers use water in their products and thus return less waste to the Sewer System than their water consumption might indicate. Upon application and approval, these commercial users are entitled to an effective rate reduction which reflects the proportion of water which is retained in their products or evaporated and not returned as sewage.

*Sewer-only Customer Charges.* In the case of premises which receive water service from alternative sources, a sewer charge is determined by DEP. For the current Fiscal Year, the sewer charge to such premises is equal to 159% of the dollar amount that would be charged for water usage if it were supplied by the Water System.

*Upstate Water Rates.* Rates for water supply service provided to municipalities and water districts located north of the City are established in accordance with the provisions of the Water Supply Act of 1905 (the “1905 Act”). The 1905 Act provides that such rates shall be based on the System’s actual cost of service. The sale of water and the rates and charges for these accounts are regulated by State law as well as by individual agreements between these communities and the City. Each contract provides for the metering of water sales to individual communities and the application of a specific charge per unit of metered volume. In most cases, per capita consumption in the upstate communities is less than that of customers within the City. In those instances where the community per capita consumption exceeds that of the City, the specified rate of charge for the excess is increased to match the rates and charges applied to retail service in the City. As of July 1, 2005, water taken from either the Croton or Catskill/Delaware systems is charged at a rate of \$617.79 per million gallons for daily per capita amounts not in excess of daily per capita consumption within the City.

*Comparative Charges.* The following table presents comparative annual water and sewer charges in 24 large cities based upon a survey conducted in March 2005. Using a ranking system where 1 represents the lowest rates, the City’s ranking relative to these cities is: for Single-Family Residential—7, for Commercial—14, and for Industrial—16.

**Comparative Annual Water and Sewer User Charges<sup>(1)</sup>**

Single Family Residential		Commercial		Industrial	
City	Annual Charge	City	Annual Charge	City	Annual Charge
Chicago <sup>(2)</sup> . . . . .	\$ 240	Chicago . . . . .	\$ 3,245	Indianapolis . . . . .	\$ 238,715
Newark . . . . .	372	Indianapolis . . . . .	3,272	Dallas . . . . .	319,592
Indianapolis . . . . .	436	Newark . . . . .	3,721	Chicago . . . . .	324,514
Milwaukee . . . . .	487	Dallas . . . . .	3,723	St. Louis . . . . .	336,599
St. Louis . . . . .	489	St. Louis . . . . .	4,107	Newark . . . . .	339,286
Baltimore . . . . .	527	Milwaukee . . . . .	4,228	Milwaukee . . . . .	343,298
<b>New York</b> . . . . .	<b>554</b>	Baltimore . . . . .	4,528	Baltimore . . . . .	397,829
Dallas . . . . .	562	Detroit . . . . .	5,075	Detroit . . . . .	397,883
Honolulu . . . . .	563	Honolulu . . . . .	5,122	Philadelphia . . . . .	431,735
Detroit . . . . .	568	Columbus . . . . .	5,214	San Antonio . . . . .	455,583
San Jose . . . . .	574	Jacksonville . . . . .	5,381	San Jose . . . . .	480,008
Columbus . . . . .	582	San Jose . . . . .	5,428	Jacksonville . . . . .	486,934
San Antonio . . . . .	614	San Antonio . . . . .	5,435	Columbus . . . . .	491,226
Jacksonville . . . . .	632	<b>New York</b> . . . . .	<b>5,540</b>	New Orleans . . . . .	492,664
Houston . . . . .	642	New Orleans . . . . .	5,881	Honolulu . . . . .	510,044
Los Angeles . . . . .	656	Los Angeles . . . . .	6,169	<b>New York</b> . . . . .	<b>554,011</b>
Cleveland . . . . .	670	Washington, D.C. . . . .	6,778	Los Angeles . . . . .	600,357
New Orleans . . . . .	691	San Diego . . . . .	6,959	San Diego . . . . .	632,692
Washington, D.C. . . . .	693	Houston . . . . .	6,981	Washington, D.C. . . . .	675,883
San Francisco . . . . .	864	Cleveland . . . . .	7,059	Houston . . . . .	682,493
San Diego . . . . .	898	Philadelphia . . . . .	7,196	Cleveland . . . . .	709,853
Boston . . . . .	925	Boston . . . . .	9,701	San Francisco . . . . .	979,763
Philadelphia . . . . .	1,036	San Francisco . . . . .	10,018	Boston . . . . .	1,037,636
Atlanta . . . . .	1,082	Atlanta . . . . .	11,899	Atlanta . . . . .	1,201,752
<b>Average</b> . . . . .	<b>\$ 640</b>	<b>Average</b> . . . . .	<b>\$ 5,944</b>	<b>Average</b> . . . . .	<b>\$ 546,681</b>

(1) User Charges are based upon information provided by the identified cities and standardized assumptions regarding water consumption, wastewater discharge, and other factors. User charges for stormwater are included in the total charges shown above for those cities with such charges. Actual charges in each city will vary in accordance with local usage patterns. Some cities bill for sewer use on the basis of winter water consumption which could affect sewer billings if a customer’s use was not uniform throughout the year. Charges for all cities reflect rate schedules in effect in March 2005.

(2) In addition to the water and sewer user charge shown above, a single family residence pays property taxes to the Metropolitan Water Reclamation District of Greater Chicago.

## **Accounts, Billing and Collection**

The Bureau of Customer Services of DEP renders bills to customers of the System and collects payments of such bills. This bureau installs and reads meters, verifies meter accuracy, and maintains current information for those customers on the flat-rate system of billing described below.

The System has approximately 824,000 water and sewer accounts, nearly all of which are for water and sewer service. Approximately 81% of the System's water and sewer customers are solely residential. The remainder are primarily commercial and industrial users, with industrial users accounting for only a small portion of water and sewer usage.

Approximately 63,000 accounts, representing 8% of total accounts, are billed annually through the flat-rate system. These accounts are charged for water either on a per unit charge or through a computation which incorporates, among other factors, the width of the front of the building ("frontage"), the number of stories, the number of dwelling units, and the number of water-using fixtures (such as bathtubs, showers and toilets) in the building. The frontage rate is computed when the building is first constructed, and amended upon notice from the City Department of Buildings ("DOB") of building alterations or when a DEP inspector determines that the basis for charges is incorrect. Flat-rate annual bills are normally sent to customers prior to the start of each Fiscal Year and are due at the end of the first month of the Fiscal Year.

Approximately 761,000 accounts, representing 92% of total accounts, are billed on a metered basis. Meters are read and billed on a quarterly basis except meters for some larger accounts which are read and billed more frequently. Most meter readings are captured electronically through the use of hand-held computers and a universal probe. Data from meter readings are relayed to computers in field offices and transmitted to a centralized computer billing system on a daily basis. Some older meters, however, must be read manually. Metered accounts are billed quarterly and bills are sent out regularly throughout the year. DEP is now testing the use of water meters that can report consumption via telephone lines transmitting data to the billing system. Unlike flat-rate charges which were commonly paid through mortgage escrow accounts, metered charges are billed directly to customers which, among other factors, has required DEP to handle a substantially higher volume of customer account inquiries. Commercial accounts are required by the Board and the City to have meters installed for all water services. Substantially all of these accounts are in compliance with this requirement.

Since 1988, the basis for service charges for residential properties has been in a continuous process of transition from a frontage or flat-rate basis of annual billing to a meter-based billing system which relies on the actual measurement of usage. The Universal Metering Program is designed to improve water conservation, water supply system management, and rate equity. The City has issued contracts for the installation of meters for the remaining unmetered accounts and is testing and replacing meters where necessary. Approximately 96% of all water and sewer accounts have meters installed. Since July 2000, unmetered properties which have not taken steps to install a meter have been required to pay a surcharge doubling their annual water and sewer charge. A surcharge was levied on approximately 12,105 accounts in their May 2005 bills.

Revenues from newly metered accounts may increase or decrease somewhat depending on how closely the flat-rate billing factors previously used compare to actual metered consumption for these accounts. Based upon recent experience, a one-time decrease in collections will occur for each account as it is metered due to the transition from billing in advance under flat rates to billing after consumption occurs. The one-time effect is taken into account in the forecasted revenues of the System.

Billing based on actual usage has affected the level of charges to certain large multiple-family residential buildings, in particular, those buildings with above-average population density and those with improperly maintained plumbing fixtures. The result is often a significant increase in charges to such buildings. In response to the needs of this segment of the customer base, the Board has adopted a transitional program whereby owners of multiple-family buildings that have had meters installed under the Universal Metering Program will continue to be billed on a flat-rate basis during the transition period.

The transitional program allows owners time to review their water usage, educate tenants regarding conservation, repair leaky plumbing, and install low-flow fixtures in order to reduce consumption and charges. There are approximately 31,700 accounts in the transitional program.

On May 11, 1993, the Board adopted a program that provides for a cap on the per-unit charge on multiple-family dwellings. The cap is set at approximately 150% of the average per-family unit charge. In order to be eligible for this program, building owners must submit to a water audit by DEP and take measures to eliminate leakage and waste.

On May 3, 2001, the Board adopted its Conservation Program for Multiple Family Residential Buildings which replaces the existing transitional program and meter billing cap program referred to above for residential buildings consisting of six or more dwelling units. It provides that owners of such buildings who replace or have replaced at least 70% of the toilet, sink and showerhead fixtures in such buildings with low-flow fixtures may elect to be billed on the basis of metered consumption or a fixed charge per dwelling unit per year. The program became effective July 1, 2001. To date, 487 applications for the program have been approved. The program is designed to be revenue neutral.

Certain institutions are exempt under State law from the payment of all or a portion of their water and sewer charges depending upon usage. These institutions include religious, certain educational and other charitable institutions as well as homes for the aged, hospitals and other non-profit or charitable corporations. For Fiscal Year 2005, metered accounts of such institutions which would be charged less than \$15,538 per year for water service are fully exempt from water and sewer charges, with a 50% exemption for those accounts ranging from \$15,538 to \$31,073 in annual water charges. There are approximately 4,000 accounts which are entirely or partially exempt from water and sewer charges.

DEP manages its account and billing information through its Customer Information System ("CIS"), which incorporates both frontage and metered accounts. DEP has identified weaknesses in the ability of the CIS to identify and report account errors and corrections on a comparable basis over time. In addition, DEP continues to issue a high percentage of estimated bills and continues to have difficulty in verifying the accuracy of a significant proportion of its overall receivable balances. DEP is working to reduce estimated bills and correct billing inaccuracies, which requires both computer analyses and an account-by-account review.

The Board and DEP have undertaken initiatives to enhance the collection of water and sewer billings. These initiatives include establishing a delinquent accounts unit for small to mid-size customers, outsourcing selected delinquency notification and collection functions to reputable collection or credit organizations, and hiring a consultant to assist in analyzing and improving collection of the accounts receivable balance. In addition, in 1999, the Board adopted a regulation authorizing DEP to terminate water and sewer services to customers because of nonpayment of assessed charges. Subject to certain notice requirements, service may be terminated if at least one delinquent charge has remained open and unpaid for at least two years, in the case of non-residential accounts and residential accounts with six or more units, or three years, in the case of residential accounts with one to five units. In May 2002, the Board approved modifications to the regulation to authorize the termination of service, subject to notice requirements, if at least one delinquent charge of at least \$1,000 has remained open and unpaid for at least one year or at least one delinquent charge of at least \$10,000 has remained open and unpaid for 90 days. The Commissioner of Finance of the City has also been authorized by the City Council in conjunction with the sale of tax liens to sell liens on behalf of the Board securing unpaid water and sewer charges. Such authorization runs through March 1, 2006.

## THE SYSTEM

### Overview

DEP supplies water and sewer service to the Boroughs of the Bronx, Brooklyn, Manhattan, Queens, Staten Island, an area of over 300 square miles, and serves over eight million people. The City is also required by State law to sell water in counties where its water supply facilities are located and where it currently provides water to an additional approximately one million people. The Water System provides an average of approximately 1,220 mgd of water. Water consumption has decreased since 1990 when an average of approximately 1,500 mgd was provided by the Water System. The amount of water that can be safely drawn from a watershed during the worst period in the drought of record is the “Dependable Yield.” DEP has determined that the System could have furnished an average of 1,290 mgd during the drought of record in the mid-1960s. During periods of normal rainfall, watersheds supply more than the Dependable Yield. The Sewer System collects and treats an average of approximately 1,300 mgd of wastewater. Sewer service is provided to virtually the entire City, except for significant parts of the Borough of Staten Island, the Borough of Queens communities of Breezy Point and Douglaston, and the Borough of Brooklyn community of Seagate. Sewer service is also provided to certain upstate communities in System watershed areas. According to Metcalf & Eddy, the System is in adequate condition (the highest rating category; see “APPENDIX A—LETTER OF METCALF & EDDY, CONSULTING ENGINEERS.”)

In recent years, DEP has taken a number of steps to enhance and augment its security arrangements to protect the System, including water supply structures and facilities. These steps include, among others, increasing the size of the DEP police force to approximately 200 officers; obtaining legislation authorizing the DEP police to function as police officers within the City, as well as in the upstate watersheds; purchasing additional police vehicles and surveillance equipment; and further securing facilities through additional locks, fences and other physical barriers to prevent access by unauthorized persons. In addition, DEP has been consulting with other governmental agencies, including the Federal Bureau of Investigation and the U.S. Army Corps of Engineers, on longer-term plans to modernize and improve security systems. In response to the attacks on the World Trade Center, DEP, in concert with law enforcement authorities, immediately implemented certain further measures to protect the System. These include, among others, increased frequency of patrols, restricting vehicular access to certain facilities, and more frequent monitoring of the water supply for contaminants. Increased security requirements have resulted in additional labor costs and related expenses in the System.

### The Water System

#### *History*

Early Manhattan settlers obtained water for domestic purposes from shallow privately owned wells. In 1677 the first public well was dug in front of the old fort at Bowling Green. In 1776, when the population reached approximately 22,000, a reservoir was constructed on the east side of Broadway between Pearl and White Streets. Water pumped from wells sunk near the Collect Pond, east of the reservoir, and from the pond itself, was distributed through hollow logs laid in the principal streets. In 1800 the Manhattan Company (now JPMorgan Chase) sank a well at Reade and Centre Streets, pumped water into a reservoir on Chambers Street and distributed it through wooden mains to a portion of the community. In 1830 a tank for fire protection was constructed by the City at 13th Street and Broadway and was filled from a well. The water was distributed through two 12-inch cast iron pipes. As the population of the City increased, the well water became polluted and supply was insufficient. The supply was supplemented by cisterns and water drawn from a few springs in upper Manhattan.

After exploring alternatives for increasing supply, the City decided to impound water from the Croton River, in what is now Westchester County, and to build an aqueduct to carry water from the Old Croton Reservoir to the City. This aqueduct, known today as the Old Croton Aqueduct, had a capacity of about 90 mgd and was placed in service in 1842. The distribution reservoirs were located in Manhattan at 42nd Street (discontinued in 1890) and in Central Park south of 86th Street (discontinued in 1925). New reservoirs were constructed to increase supply: Boyds Corner in 1873 and Middle Branch in 1878. In 1883



a commission was formed to build a second aqueduct from the Croton watershed as well as additional storage reservoirs. This aqueduct, known as the New Croton Aqueduct, was under construction from 1885 to 1893 and was placed in service in 1890, while still under construction.

Since 1842, there have been no significant interruptions of service.

In 1905 the Board of Water Supply was created by the State Legislature. Pursuant to the 1905 Act, the City may develop areas of the Catskill Mountains, located in the Hudson River Basin, and portions of the Delaware River Basin located to the west of the Catskill Mountains for water supply purposes. In return for these development rights, the 1905 Act requires the City to furnish, upon request, supplies of fresh water to municipalities and water districts in eight northern counties in which City water supply facilities and watersheds are located. The City's obligations under the 1905 Act in this respect have now passed to the Board. The 1905 Act also governs the rates that may be levied for such water. An eligible municipality or district may draw water based on a formula computed as the local population multiplied by the daily per capita consumption in the City. The City is currently engaged in a long-term project to update and modernize various water supply agreements governing the furnishing of water to such municipalities and water districts.

After careful study, the City decided to develop the Catskill region as an additional water source. The Board of Water Supply proceeded to plan and construct facilities to impound the waters of the Esopus Creek, one of the four watersheds in the Catskills, and to deliver the water throughout the City. This project, to develop what is known as the Catskill System, included the Ashokan Reservoir and the Catskill Aqueduct and was completed in 1915. It was subsequently turned over to the City's Department of Water Supply, Gas and Electricity for operation and maintenance. The remaining development of the Catskill System, involving the construction of the Schoharie Reservoir and Shandaken Tunnel, was completed in 1928.

In 1927 the Board of Water Supply submitted a plan to the Board of Estimate and Apportionment for the development of the upper portion of the Rondout watershed and tributaries of the Delaware River within the State of New York. This project was approved in 1928. Work was subsequently delayed by an action brought by the State of New Jersey in the Supreme Court of the United States to enjoin the City and State of New York from using the waters of any Delaware River tributary. In May 1931 the Supreme Court of the United States upheld the right of the City to augment its water supply from the headwaters of the Delaware River. Construction of the Delaware System was begun in March 1937. The Delaware System was placed in service in stages: The Delaware Aqueduct was completed in 1944, Neversink Reservoir in 1950, Rondout Reservoir in 1951, Pepacton Reservoir in 1954 and Cannonsville Reservoir in 1967.

Water for the System is derived from three upstate reservoir systems (the Croton, Catskill and Delaware Systems) and a system of wells in Queens that were acquired as part of the City's acquisition of the Jamaica Water Supply Company ("Jamaica Water"). The three upstate water collection systems include 18 reservoirs and three controlled lakes with a total storage capacity of approximately 550 billion gallons. They were designed and built with various interconnections to increase flexibility by permitting exchange of water from one system to another. This feature mitigates localized droughts and takes advantage of excess water in any of the three watersheds.

The Water System is currently furnishing water to users in portions of four of the eight eligible northern counties. The Water System provides approximately 85% of the water used in Westchester County and approximately 7.5% of the water used in Putnam, Orange and Ulster Counties.

Approximately 95% of the total water supply is delivered to buildings by gravity. Only about 5% of the water is regularly pumped by DEP to maintain the desired pressure. As a result, operating costs are relatively insensitive to fluctuations in the cost of power. When drought conditions exist, additional pumping is required.

#### *Water Collection and Distribution*

The three main reservoir systems are the Croton, Catskill and Delaware Systems. See "New York City Water Supply System" map in Appendix H.

The following tables set forth the capacities and original in-service dates of the System's collecting and balancing reservoirs and distribution facilities based on the City records.

### Collecting Reservoirs

<u>Name</u>	<u>Available Capacity(1) (Billion Gallons)</u>	<u>Original In-Service Date</u>
<b>Croton</b>		
New Croton.....	19.0	1905
Croton Falls Main.....	14.2	1911
Cross River.....	10.3	1908
West Branch.....	10.1	1895
Titicus.....	7.2	1893
Amawalk.....	6.7	1897
East Branch.....	5.2	1891
Muscoot.....	4.9	1905
Bog Brook.....	4.4	1892
Middle Branch.....	4.0	1878
Boyds Corner.....	1.7	1873
Croton Falls Diverting.....	<u>0.9</u>	1911
Total.....	88.6	
<b>Catskill</b>		
Ashokan.....	122.9	1915
Schoharie.....	<u>17.6</u>	1926
Total.....	140.5	
<b>Delaware</b>		
Pepacton.....	140.2	1955
Cannonsville.....	95.7	1964
Rondout.....	49.6	1950
Neversink.....	<u>34.9</u>	1954
Total.....	<u>320.4</u>	
Total Available Capacity.....	<u><u>547.5</u></u>	

(1) Capacity above minimum operating level.

## Balancing Reservoirs and Distribution Facilities

<u>Name</u>	<u>Storage Capacity (billion gallons)</u>	<u>Original In-Service Date</u>
<b>Balancing Reservoirs</b>		
Kensico .....	30.6	1915
Hillview .....	<u>0.9</u>	1915
Total Balancing Reservoirs.....	31.5	
<b>Distribution Facilities</b>		
Central Park .....	1.0	1862
Jerome Park .....	0.8	1905
Silver Lake (tanks) .....	<u>0.1</u>	1970
Total Distribution Facilities .....	<u>1.9</u>	
Total Storage Capacity .....	<u><u>33.4</u></u>	

The following table sets forth the Dependable Yield and storage capacity for each of the water supply systems.

### Water System Dependable Yield and Capacity

<u>System</u>	<u>Dependable Yield (mgd)</u>	<u>Storage Capacity(1) (billion gallons)</u>
Croton .....	240	86.6
Catskill.....	470	140.5
Delaware.....	580	320.4
Queens wells.....	<u>33</u>	<u>2.6</u>
Total.....	<u><u>1,323</u></u>	<u><u>550.1</u></u>

(1) Capacity above minimum operating level.

The Croton System normally provides approximately 10% of the City's daily water supply and can provide substantially more of the daily water supply during drought conditions. The Croton System consists of 12 reservoirs and three controlled lakes on the Croton River, its three branches and three other tributaries. The water in the Croton System flows from upstream reservoirs through natural streams to downstream reservoirs, terminating at the New Croton Reservoir. The watershed which supplies the Croton System has an area of 375 square miles. It lies almost entirely within the State, approximately 45 miles north of lower Manhattan, with a small portion in the State of Connecticut.

The Catskill System watersheds occupy sparsely populated areas in the central and eastern portions of the Catskill Mountains and normally provide approximately 40% of the City's daily water supply. Water in the Catskill System comes from the Esopus and Schoharie Creek watersheds, located approximately 100 miles north of lower Manhattan and 35 miles west of the Hudson River. The Catskill System is comprised of the Schoharie Reservoir (formed by the Gilboa Dam across Schoharie Creek) and Ashokan Reservoir (formed by the Olivebridge Dam across Esopus Creek) and the Catskill Aqueduct.

The Delaware System, located approximately 125 miles north of lower Manhattan, normally provides approximately 50% of the City's daily water supply. Three Delaware System reservoirs collect water from a sparsely populated region on the branches of the Delaware River: Cannonsville Reservoir (formed by the Cannonsville dam on the West Branch of the Delaware River); Pepacton Reservoir (formed by the Downsview Dam across the East Branch of the Delaware River); and Neversink Reservoir (formed by the Neversink Dam across the Neversink River, a tributary to the Delaware River).

In addition, wells in Queens provide approximately 1% of the City's daily water supply. The wells could be used to provide more of the daily supply during drought conditions. Unlike the rest of the City's water supply, which is a surface and gravity-supplied system originating in a network of upstate reservoirs, well water is pumped from extensive underground aquifers. The acquisition of wells in Queens from Jamaica Water in 1996 represented the first new water supply source for the City since the 1960s when the Delaware surface water system initially came on line. DEP is currently planning improvements to the ground water system which will augment the supply of water from underground aquifers.

Current demand/flow projections show that if conservation programs, including metering, toilet replacement, hydrant locking, leak detection, and public information, remain effective there will be no immediate need for the City to find additional long-term water supply sources to meet normal demand.

The System's water supply is transported through an extensive system of tunnels and aqueducts. See "New York City Water Tunnels" map in Appendix H. Croton System water is delivered from the New Croton Reservoir by the New Croton Aqueduct to the Jerome Park Reservoir in the Bronx. From Jerome Park Reservoir and from direct connections to the New Croton Aqueduct, trunk mains carry water to the service area. The Catskill and Delaware Aqueducts convey water from Ashokan Reservoir and Rondout Reservoir to Kensico Reservoir and then to Hillview Reservoir in Yonkers. Both Kensico and Hillview Reservoirs serve as balancing reservoirs. Water from the Catskill and Delaware Systems is mixed in the Kensico Reservoir, and is conveyed to Hillview Reservoir where water enters Tunnels 1, 2 and 3. Trunk mains carry water from tunnel shafts and from the distribution facilities (Jerome Park and Hillview Reservoirs and Silver Lake Tanks) to the service area.

DEP regularly assesses the condition and integrity of the System's tunnels and aqueducts to determine the extent and effect of water loss. In particular, DEP is focusing on an assessment of the condition of the Rondout-West Branch Tunnel, which comprises a portion of the Delaware Aqueduct. The Rondout-West Branch Tunnel carries water 45 miles from the Delaware System under the Hudson River and into West Branch Reservoir. It has a capacity of 900 mgd and normally contributes 50% of the City's water supply. It is unique in that it has the highest pressures and the highest velocities in the Water System. In addition, a portion of the tunnel crosses a fractured rock formation, which is potentially subject to greater stress than the deep rock tunnels located in the City. Since the early 1990s, DEP has monitored the condition of the Rondout-West Branch Tunnel. As a result of DEP's flow tests, visual observations and other analyses conducted over the last five years, it has been determined that between approximately 15 mgd and approximately 36 mgd of water is being lost from the tunnel and is surfacing in the form of springs or seeps in the area. This amounts to a loss of approximately 4% of the daily volume of water provided by the tunnel under peak flow conditions. DEP has initiated the engineering work to determine the nature and extent of repairs which may be necessary to remedy the water loss. DEP has also determined that the situation in the tunnel and amount of water loss is stable and that, in the opinion of the professional engineering firm retained by DEP in conjunction with that investigation, there is very little immediate risk of failure of the tunnel. DEP intends to make the necessary repairs. The costs to perform such repairs could be substantial depending on the nature of the required repair. To perform the repair work, the tunnel will probably have to be shut down and de-watered. During any such period, it will be necessary for the City to increase reliance on its other water supplies, and to implement more stringent measures to encourage conservation and decrease demand. Under an extended shutdown of this tunnel, water quality in the remaining reservoirs could potentially suffer as storage volumes are drawn down. In general, the Delaware System continues to demonstrate a high degree of reliability after 55 years of continuous service. Nevertheless, DEP considers it prudent to conduct regular tunnel and aqueduct inspections and surveys to detect any problems that might arise so that corrective actions can be taken if needed.

DEP has begun to evaluate additional strategies and projects for improving dependability of supplies when various facilities or portions of the overall Water System may have to be taken out of service for extended periods of time for either planned or unplanned inspection, repair or rehabilitation. Such strategies or projects could entail the development of additional or interim supplies to meet demands during periods of extended facility outages. DEP has entered into a consultant contract to develop a long term dependability plan. That contract is intended to evaluate various alternative projects which, when

combined, could allow for any portion of the Water System to be taken out of service for a period of up to one year. A draft dependability plan could be proposed within two years. Elements of that plan may include: interconnections with other neighboring jurisdictions; increased use of groundwater supplies; storage and recovery of existing supplies within underground aquifers; increased storage at existing reservoirs; withdrawals and treatment from other surface waters; hydraulic improvements to existing aqueducts; and additional tunnels.

*Tunnel 1.* From Hillview Reservoir, water from the Catskill and Delaware Systems is delivered into the City by a circular, cement-lined, pressurized, bedrock tunnel that narrows in diameter from 15 to 11 feet. Tunnel 1 is 18 miles in length and extends south from Hillview Reservoir through the West Bronx to Manhattan and Brooklyn. Tunnel 1 is 200 to 750 feet underground and thus avoids interference with streets, buildings, subways, sewers, pipes and other underground infrastructure. These depths are necessary to ensure substantial rock covering necessary to withstand the bursting pressure of the water inside and to ensure watertightness. Tunnel 1 has a capacity of approximately 1,000 mgd. Shafts placed along the tunnel connect with surface mains which deliver water to the distribution system.

*Tunnel 2.* The second tunnel also delivers Catskill and Delaware System water from Hillview Reservoir. It is a circular, cement-lined, pressurized, bedrock tunnel, 200 to 800 feet below the street surface and 15 to 17 feet in diameter. Tunnel 2 extends south from Hillview Reservoir, east of Tunnel 1, through the Bronx, under the East River at Rikers Island, through Queens and Brooklyn, and connects with Tunnel 1 in Brooklyn. Tunnel 2 has a capacity of more than 1,000 mgd and is 20 miles in length. Shafts placed along the tunnel connect with surface mains which deliver water to the distribution system.

*Richmond Tunnel.* Connecting to Tunnel 2 in Brooklyn is the ten-foot diameter, five-mile long Richmond Tunnel, which was completed in 1970 and carries water 900 feet beneath Upper New York Bay to Staten Island. The Richmond Tunnel, the Richmond Distribution Chamber, the Richmond Aqueduct and the underground Silver Lake Tanks were designed to improve the water supply facilities of Staten Island. The underground storage tanks (among the world's largest) have a combined capacity of 100 million gallons and replaced the Silver Lake Reservoir (now Silver Lake).

*Tunnel 3.* A new water tunnel, Tunnel 3, connecting the reservoir system to the City is presently under construction to increase capacity to meet a growing demand in the eastern and southern areas of the City, permit inspection and rehabilitation of Tunnels 1 and 2, and provide water delivery alternatives to the City in the event of disruption in Tunnel 1 or 2. Tunnel 3 is being built in four stages. Stage I commenced operation in July 1998. It follows a 13-mile route which extends south from Hillview Reservoir in Yonkers under Central Park Reservoir in Manhattan, and east under the East River and Roosevelt Island to Long Island City in Queens. Stage II is currently under construction and is expected to be completed in 2012. It will extend from the end of Stage I to supply Queens, Brooklyn and the Richmond Tunnel and from the valve chamber at Central Park into lower Manhattan. Upon completion, and with the installation of additional surface mains, Stage II will enable the system to maintain full service even if Tunnel 1 or 2 was shut down. The Stage III project is now referred to as the Kensico-City Tunnel (the "Kensico Tunnel"). Stage IV is intended to deliver additional water to the eastern parts of the Bronx and Queens. It would extend southeast from the northern terminus of Stage I in the Bronx to Queens and then southwest to interconnect with the Queens portion of Stage II.

*Kensico-City Tunnel.* The Kensico-City Tunnel will extend from the Kensico Reservoir to the interconnecting chamber of Tunnel 3, Stage I, south of Hillview Reservoir. \$1.7 billion is included for the project in the CIP.

The water distribution system consists of a grid network of over 6,200 miles of pipe, as well as valves, fire hydrants, distribution facilities, gatehouses, pump stations, and maintenance and repair yards. Some pipe was installed before 1870 and approximately 6.5% is over 100 years old. Approximately 2,000 miles of pipe are unlined cast iron laid before 1930. Pipe laid between 1930 and 1969 is cement-lined cast iron and comprises about 2,300 miles of the distribution system. Pipe laid after 1970 is cement-lined ductile iron and comprises about 1,900 miles of the distribution system. The CIP provides for the programmatic replacement of water mains in accordance with certain established criteria. These criteria were reviewed and confirmed by the U.S. Army Corps of Engineers in its independent study of the City's distribution system completed in November 1988.

Various facilities provide storage to meet the hourly fluctuations in demand for water throughout the City, as well as any sudden increase in draft that might arise from fire or other emergencies. With the exception of some communities in the outlying areas of the City which may experience low pressure service during peak hours in summer months, the water distribution system provides generally excellent service.

### *Drought Response Measures*

From time to time the Water System experiences drought conditions caused by significantly below-normal precipitation in the watershed areas. A Drought Watch (as defined herein) was declared in late December 2001, a Drought Warning (as defined herein) was declared in late January 2002 and a Drought Emergency (Stage I) (as defined herein) was declared in March 2002. In November 2002, the City downgraded the Drought Emergency to a Drought Watch and in January 2003 the Drought Watch was lifted. As of October 18, 2005, the System's reservoirs were filled to 75% of capacity. Normal levels at this time of year would be approximately 72% of capacity.

The Water System relies upon a surface water supply, and is sensitive to major fluctuations in precipitation. Throughout even the worst droughts, the Water System has continued to supply sufficient amounts of water to the City. To ensure adequate water supply during drought conditions, DEP, in conjunction with other City, State and interstate agencies, maintains a Drought Management Plan. The Drought Management Plan defines various drought phases that trigger specific management and operational action. Three defined phases are: "Drought Watch," "Drought Warning," and "Drought Emergency." A Drought Emergency is further subdivided in four stages based on the projected severity of the drought and provides increasingly stringent and restrictive measures.

A Drought Watch is declared when there is less than a 50% probability, based on the existing record since 1927, that either the Catskill or Delaware reservoir system will be filled by the following June 1. This phase initiates the pumping of water from the Croton System. In addition, during this phase a public awareness program begins and users, including upstate communities taking water from the System, are requested to initiate conservation measures. NYSDOH, NYSDEC, and the Delaware River Basin Commission (the "DRBC") are advised of the Water System's status, and discussions are held with City agencies concerning their prospective participation in the event of a declaration of a Drought Warning.

A Drought Warning is declared when there is less than a 33% probability that either the Catskill or Delaware reservoir system will fill by June 1. All previous efforts are continued or expanded and additional programs are initiated, including the coordination of specific water saving measures by other City agencies.

A Drought Emergency is declared when it becomes necessary to reduce consumption by imposing even more stringent measures. In addition to the imposition of restrictions, DEP may enhance existing System management and public awareness programs, expand its inspection force and perform additional leak and waste surveys in public and private buildings. DEP may also require communities outside of the City that are served by the System to adopt similar conservation measures. During several drought emergencies, DEP has operated the Chelsea Pump Station which can draw up to 100 mgd from the Hudson River. However, DEP has committed not to use the Chelsea Pump Station in its planning for future emergencies.

### *Governmental Regulation*

The System is subject to federal, State, interstate and municipal regulation. At the federal level regulatory jurisdiction is vested in USEPA; at the State level in NYSDEC and NYSDOH; at the interstate level in the DRBC and the Interstate Environmental Commission and at the municipal level in DEP, NYCDOH, DOB and the Department of Business Services and to a limited degree, in municipalities and districts located in eight counties north of the City. Water quality standards are enforced within the watershed areas north of the City through a network of overlapping governmental jurisdictions. Participating in that network, among others, are NYSDEC and NYSDOH, county, municipal and district police, engineers and inspectors; and City personnel from DEP. The various jurisdictions maintain

physical security, take water samples, monitor the use of herbicides, insecticides and fertilizers, and generally oversee the physical condition of, activity on and the operation of water supply lands and facilities. Portions of the overall legislative and regulatory framework governing the watersheds may be found in the City's Administrative Code, Health Code and Water Supply Regulations. Regulatory enforcement within City limits is almost exclusively accomplished through City personnel. Provisions incorporating and augmenting the substance of the federal Safe Drinking Water Act ("SDWA"), related regulations and the Sanitary Code, are contained in the Health Code, Water Supply Regulations and the City's Building and Building Construction Codes. These provisions are enforced by personnel from DEP, NYCDOH and DOB.

It is anticipated that during the spring of 2006 USEPA will promulgate two new rules under the SDWA with respect to disinfection that may require DEP to change certain aspects of its disinfection procedures and may increase costs to the Water System.

*Croton Filtration.* Because of the quality of the System's water and the long periods of retention in the reservoirs, it has not been necessary to filter water from the System to reduce the bacterial content and the turbidity. The only treatment procedures routinely employed by DEP are screening, detention, disinfection, fluoridation, and the addition of caustic soda and phosphoric acid for corrosion control. Additions of copper sulfate for algae control and alum for turbidity control are made only when needed. This level of treatment proved to be more than sufficient to maintain water quality standards throughout the entire Water System. However, new water treatment standards led to a 1992 stipulation with NYSDOH which provided for the construction of a full scale water treatment facility to filter Croton System water. The stipulation has been superceded by a 1998 federal court consent decree (the "Croton Filter Consent Decree"). The Croton Filter Consent Decree sets forth milestones which, if not met by the City, require the payment of penalties to the State and federal governments.

In December 1998, after an extensive study of several alternative sites, DEP identified the Mosholu Golf Course in the Bronx as the City's preferred site for the full-scale water treatment facility to filter Croton System water. The selected Mosholu Golf Course site lies within the boundaries of Van Cortlandt Park, a mapped public park. Actions brought against the City resulted in a February 2001 New York Court of Appeals decision that the construction and operation of a Croton water treatment facility at this site would constitute an alienation of parkland by the City, requiring State legislative approval. On July 22, 2003, the proposed alienation legislation was enacted into law. On June 30, 2004, DEP issued a final supplemental environmental impact statement which identified the Mosholu Golf Course site as the preferred site.

The City has entered into two supplements to the Croton Filter Consent Decree with USEPA and the State. The Second Supplement, which was entered by the United States District Court on January 27, 2005, provides for consideration of siting the Croton filtration facility at the three potential sites, including a site located alongside the Harlem River in the vicinity of Fordham Road (by 2012), a site in Westchester County located on City-owned property in the Town of Mount Pleasant (by 2010) and the Mosholu Golf Course site (by 2011). The City began work at the Mosholu Golf Course site in late 2004. The Second Supplement also provides for the payment by the City of \$185,000 in penalties for having missed the April 30, 2003 milestone set forth in the First Supplement. It also provides that the City pay reasonable fees and expenses, up to \$225,000, of an engineering consultant to be engaged by USEPA and the State to review the City's schedule for construction of the Croton filtration plant and the feasibility of accelerating its completion. The total estimated cost of the Mosholu Facility is \$1.5 billion, which is included in the CIP. For information about four lawsuits seeking to enjoin construction of the Croton filtration plant at the Mosholu Golf Course site, see "LITIGATION."

In the second quarter of 2003, the Croton System exceeded the water quality standard for haloacetic acids, a disinfection by-product regulated by USEPA. On June 19, 2003, USEPA issued an administrative order requiring DEP to inform consumers about the violation and to propose feasible and cost effective measures to reduce haloacetic acid levels until the Croton filtration plant is completed. DEP distributed the required public notice to Croton System consumers on July 15, 2003 and submitted the required evaluation of potential interim measures to USEPA and NYSDOH on August 4, 2003. DEP is conducting additional analyses to determine which measures will be most efficacious and cost-effective.

*Watershed Protection/Catskill, Delaware Filtration.* Pursuant to the SDWA, USEPA has promulgated nationwide drinking water regulations which specify the maximum level of harmful contaminants allowed in drinking water and which govern the construction, operation, and maintenance of the System. USEPA has also promulgated filtration treatment regulations, known as the federal Surface Water Treatment Rule (“SWTR”), that prescribe guidelines concerning studies to be performed, programs to be implemented, timetables to be met and any other actions necessary to insure compliance with the regulations’ terms. Enforcement of SDWA and its related regulations, except for the SWTR, was delegated by USEPA to the State. USEPA has delegated primary enforcement responsibility for the SWTR to NYSDOH for all systems in the State other than the Catskill and Delaware Systems. With respect to the Catskill and Delaware systems, the City believes that under the SWTR promulgated by the USEPA it will continue to be able to meet the criteria for non-filtered supplies.

On January 21, 1997, the City and the State executed a Memorandum of Agreement with the communities in the Catskill, Delaware and Croton watersheds, USEPA and several environmental groups (the “Watershed Memorandum of Agreement”). The Watershed Memorandum of Agreement supplemented the City’s existing watershed protection program with approximately \$400 million in additional funding. This funding, at least \$290 million of which is expected to be provided through the issuance of Authority bonds, consists of \$350 million for economic-environmental partnership programs with upstate communities which include a water quality investment program, a regional economic development fund and a regional advisory forum for water quality initiatives and watershed concerns. As provided under the Watershed Memorandum of Agreement, the State has issued a land acquisition permit to the City to acquire water quality sensitive land in the watershed and has approved the City’s revised rules and regulations governing certain aspects of land use in the watershed. The State also promulgated the same regulations under state law procedures in July 1998.

Since 1993, USEPA has issued filtration avoidance determinations (“FADs”) pursuant to which the City is not required to filter water from the Catskill and Delaware Systems. If the City were to have to filter water from the Catskill and Delaware Systems, current estimates of the construction costs to provide for such filtration are approximately \$3 billion. On November 26, 2002, USEPA announced the issuance of a new FAD which supersedes previous determinations and will remain in effect until further determination is made, now scheduled for April 2007 (the “2002 FAD”). The 2002 FAD requires that the City take certain actions over the next two years to protect the Catskill and Delaware water supplies and justify the continuation of filtration avoidance. These actions include the continuation and enhancement of certain environmental and economic partnership programs established under the Watershed Memorandum of Agreement, and the creation of new programs. The 2002 FAD requires, among other things, continuation of the program for repair and rehabilitation of certain watershed septic systems, construction of an ultraviolet treatment facility (the “UV facility”) to be operable by September 2009, development of a new Community Wastewater Management Program, the continuation of the Stormwater Retrofit Program, and continuation of the Stream Management Program. In addition, the 2002 FAD requires upgrades to approximately 25 non-City owned wastewater treatment plants by varying dates, the latest of which is November 15, 2004, and the connection of certain other existing plants to new plants to be constructed under the New Infrastructure Program by the first half of 2005. The upgrades of certain small wastewater treatment plants located on the west side of the Hudson River, which account for less than 2% of the wastewater flow in the Catskill and Delaware watersheds and whose upgrades are mandated by the 2002 FAD, have been delayed until 2006 due to delays in finalizing upgrade designs. USEPA is aware of these schedule changes. Capital costs associated with the 2002 FAD, excluding the UV facility, are estimated to be approximately \$163 million, and are included in the CIP. Approximately \$634 million has been included in the CIP for the UV facility. USEPA has granted an extension of 14 additional months, until November 2010, to put the UV facility into service and will amend the FAD to include the new date. In exchange, the City has agreed to provide an additional \$6 million in funding to the Community Wastewater Management Program.

In addition, the 2002 FAD continues the requirement that the City solicit property from owners of 355,050 acres of land in the watershed and actually acquire (with certain limited exceptions) title to or conservation easements on any land used to satisfy the solicitation goal where the owner accepts the City’s



purchase price. In particular, the City must continue to aggressively pursue additional land acquisition in the Kensico Reservoir basin. To be eligible for acquisition, land must satisfy specified natural features and minimum acreage criteria. The Watershed Memorandum of Agreement required the City to set aside \$250 million for land acquisition, with an option to increase the funding by up to \$50 million (“Supplemental Land Funds”). The 2002 FAD requires the City to confer with USEPA and NYSDOH biannually commencing in January 2004, on the need for allocating all or a portion of the Supplemental Land Funds. As required, the City met with USEPA and NYSDOH in January 2004, and as a result USEPA has directed the City to allocate an additional \$7 million to its watershed land acquisition program, for the purpose of acquiring agricultural easements on farm properties in the watershed. The City will confer with USEPA and NYSDOH again in January 2006, regarding the need to supplement the acquisition program with the remaining \$43 million in Supplemental Land Funds. Pursuant to the Watershed Memorandum of Agreement, in 1997 NYSDEC issued a land acquisition permit to the City that had a term of 10 years with an option to extend for five years. The 2002 FAD requires the exercise of the option for the five years which would extend the permit to 2012. As of August 31, 2005, the City has either acquired, or has contracts to acquire, title to or conservation easements on approximately 65,000 acres of land in the Catskill and Delaware watersheds with an aggregate value of approximately \$158 million.

*USEPA/U.S. Attorney Investigations.* On August 23, 2001, DEP resolved a criminal investigation by USEPA and the United States Attorney’s Office in the Southern District of New York concerning the presence of mercury, PCBs and lead at several DEP facilities in the watershed. Under the resolution, DEP pled guilty to a felony violation of the Clean Water Act and a misdemeanor violation of the federal Toxic Substances Control Act and paid a fine of \$50,000. DEP also accepted oversight of elements of the System by a court-appointed monitor and was placed on probation, both for a term of three years, extendable by the court for up to two additional years. On May 19, 2004, with the consent of DEP, the court extended probation and the appointment of the monitor for one year, through August 29, 2005. In July 2005, DEP again consented to the court extending probation and the appointment of the monitor for another year, through August 29, 2006. On July 14, 2005, the U.S. Department of Probation filed a petition in court alleging that DEP violated the terms of its probation when a DEP manager attempted to impede an audit of a DEP facility by the monitor’s consultants and when a DEP employee made false entries into a DEP logbook. DEP has admitted the violations. On September 22, 2005, with DEP’s concurrence, the court entered an order directing DEP to undertake certain measures to address probation violations. These measures include developing a complaint procedure to better address certain types of employee concerns; distributing a notice to all employees explaining the function of the court-appointed monitor, the obligation of employees to cooperate with the monitor, and the availability of employee complaint procedures; and thoroughly reviewing certain water quality sampling, testing, recordkeeping and reporting procedures used to comply with the SDWA and the State Sanitary Code.

The Clean Water Act violation, to which DEP pled guilty is based on the discharge of water containing low levels of mercury from a DEP facility in Sullivan County. The Toxic Substances Control Act violation is based on DEP’s use of flow control equipment which contains PCBs in other than a totally enclosed manner at a facility in Westchester County. The conditions which gave rise to the violations have not had any detectable impact on water quality and the City’s water supply has been, and continues to be, safe and wholesome. The federal government, NYSDOH and DEP have all indicated that the water supply remains safe with respect to mercury, PCBs and lead. DEP has been and continues to be engaged in programs to remediate mercury, PCBs, lead, and other constituents of concern from the affected facilities. DEP’s operation and management of the System will not materially change as a result of the plea.

On August 14, 2003, the City (along with major portions of the northeastern United States) experienced a massive power blackout. With the loss of electrical power during the blackout, DEP’s North River and Red Hook water pollution control plants were unable to treat wastewater being conveyed to those facilities, resulting in the outflow of untreated wastewater into the waters of New York Harbor. The United States Attorney’s Office for the Southern District of New York is investigating this matter and, beginning in November 2003, issued a series of subpoenas to DEP for information and documents

pertaining to back-up and emergency power systems at the North River and Red Hook plants, and has questioned certain DEP employees and has had certain DEP employees testify before a grand jury. DEP is cooperating with this investigation and is providing information and documents in response to such subpoenas.

DEP has historically monitored key locations in its distribution system for over 40 individual water quality parameters, including lead. DEP data indicated that lead was absent from or present in very low levels in both the water supply and distribution systems. Beginning in the early 1990s, USEPA and NYSDOH regulations require water suppliers to monitor for lead and copper that may have leached into the water from service lines or interior building plumbing. In compliance with these requirements, DEP began testing tap water for lead and copper. Sample results indicated the presence of lead in some of the tested residential taps, in excess of State lead action levels. To minimize these occurrences, the City began the addition of corrosion control chemicals to the Water System. This addition promotes the formation of a protective coating inside pipes and plumbing, thereby reducing the leaching of metals. Since the second quarter of 1999, DEP has reported its tap water sampling to be in compliance with State action levels for lead.

On October 6, 2004, the United States Attorney's Office for the Southern District of New York began investigating DEP's compliance with State and federal lead regulations governing reporting of lead levels in tap water and has issued two subpoenas to DEP requesting documents pertaining to the sampling and reporting of tap water for the presence of lead. DEP cooperated with the investigation. In early February 2005, the United States Attorney's Office advised the City that it was no longer pursuing the investigation.

In November 2004, after receiving certain additional information requested from DEP on testing for lead in tap water, NYSDOH issued a Notice of Violations to DEP, alleging that the City had violated the Lead and Copper Rule provisions of the State Sanitary Code by failing to report certain lead testing data, by not including certain test results in calculations used to determine compliance with such provisions, and by failing to collect certain lead tap samples. Based on the information provided by DEP, NYSDOH alleged that the City was out of compliance with the action level for lead set forth in the State Sanitary Code during certain reporting periods where the City had claimed to be in compliance. NYSDOH directed DEP to undertake certain actions to address these alleged violations, including re-institution of DEP's public education program on lead in drinking water, conducting more frequent monitoring for lead, and initiating a lead service line replacement program of city-owned buildings.

The Lead and Copper Rule provisions of the State Sanitary Code are complex and are susceptible to differing interpretations with respect to the sampling results that must be included in calculating compliance with the rule. NYSDOH's allegations are based on an interpretation that differs from that which has been consistently followed by DEP for many years. As such, although DEP disputes a number of the conclusions drawn by NYSDOH in the Notice of Violations, DEP is working with NYSDOH and with the City's Department of Health and Mental Hygiene, to improve and enhance its lead testing programs. These improvements include, among others, the preparation of detailed written protocols on how testing for lead in tap water will be conducted and how the results will be reported, the collection of data to determine where lead service lines exist within the City, and the prioritization of lead service lines in city-owned buildings for potential replacement. The most recent test results for lead in tap water, for 2003 and 2004, show the City to be in compliance with the action level for lead in the State Sanitary Code.

The System has six laboratories that monitor water quality, employing approximately 250 microbiologists, engineers, chemists, hydrologists and limnologists. Over 65,000 samples per year are collected and 800,000 analyses are performed annually. Routine checks are made for more than 60 different substances, including heavy metals and trace organics. The monitoring program meets or exceeds federal and State requirements and has the capability to meet potentially more stringent requirements.

From time to time, the United States Attorney's Office requests additional information from DEP concerning the System, and issues subpoenas for additional documents. DEP cooperates with the office and provides information and documents in response to such requests and subpoenas.

*Hillview Reservoir.* In March 1996, DEP entered into an Administrative Order with NYSDOH which required, among other things, that the City install or construct a cover for the Hillview Reservoir

to reduce the possibility of E. coli bacteria entering the Water System. The Administrative Order was modified in July 1997 and March 1999. As modified, it requires that the City complete installation or construction of the selected cover for Hillview Reservoir by December 31, 2005.

Over the past three years, DEP has conducted studies and has held discussions with NYSDOH to evaluate other strategies, including more aggressive waterfowl control, to protect the Hillview Reservoir. Although DEP believes that certain other strategies hold promise, DEP was advised by NYSDOH, in August 2001, that the Administrative Order will not be modified in this respect and that the City must cover Hillview Reservoir in accordance with the terms of the Order. DEP has renewed discussions with NYSDOH on modifications to the Administrative Order based on its overall water supply plan and possible scheduling conflicts with other water supply projects. While these discussions are proceeding, NYSDOH is requiring DEP to pay stipulated penalties into an escrow account as set forth in the Administrative Order. The estimated cost of a Hillview Reservoir cover is approximately \$400 million which is not included in the CIP. However, DEP has provided \$258 million in the CIP to upgrade Hillview Reservoir facilities to implement certain alternative strategies including aggressive water fowl control, increased security and other facility modifications.

*Consumer Confidence Report.* The SDWA requires that utilities prepare and distribute to their consumers a brief annual water quality report, referred to as the Consumer Confidence Report (the “CCR”). The CCR covering calendar year 2004, the most recent such report, demonstrates that the quality of New York City’s drinking water remains high. The CCR noted that in the first quarter 2004, the Croton system violated the maximum contaminant level for haloacetic acids. The Croton filtration project is intended, among other things, to address the issue of haloacetic acid contamination in the Croton system water. The CCR further noted several exceedences of standards of naturally-occurring elements iron and manganese, as well as a Croton system violation of the color standard. None of these exceedences are considered harmful to public health. In addition, DEP received a Notice of Violation from NYSDOH for failure to accurately report results of monitoring at-the-lap lead concentrations for two consecutive monitoring periods (discussed in more detail above).

*Delaware System.* The conditions under which the System’s Pepacton, Neversink and Cannonsville Reservoirs may be operated are set forth under the terms of a 1954 decree of the Supreme Court of the United States (the “1954 Decree”). It allows the System to divert 800 mgd of water from the Delaware River Basin for use by the Water System. At the same time, the System is required to release, from the three reservoirs into the tributaries of the Delaware River, quantities of water sufficient to maintain flows of 1,750 cubic feet per second in the main branch of the Delaware River at Montague, New Jersey. In addition, the System must meet the State-mandated conservation releases and flow requirements in various tributaries contained in numerous deeds and condemnation decrees. Enforcement of the 1954 Decree is under the jurisdiction of a River Master appointed by the Supreme Court of the United States. The City and State, and the governments of New Jersey, Pennsylvania and Delaware are named parties to the 1954 Decree.

The DRBC was created in 1961 as a result of the Delaware River Basin Compact among the federal government, the State, and the states of New Jersey, Pennsylvania and Delaware. It has jurisdiction over water resources and is responsible for development, planning and coordination and protection of the interstate areas served by the Delaware River and its tributaries. Although not a participant in the Delaware River Basin Compact, the City functions as an advisor to the State in DRBC proceedings and assumes a major role both as a party to the 1954 Decree and as the owner and operator of the three largest reservoirs subject to DRBC jurisdiction.

In 1982, as a result of conditions during the drought of record in the mid-1960s, the drought of 1981, and the inability of the System’s Pepacton, Neversink and Cannonsville Reservoirs to satisfy all of the requirements of the 1954 Decree during those drought periods, a set of Interstate Water Management Recommendations (the “Good Faith Agreement”) was submitted to DRBC. Executed by all of the parties to the 1954 Decree, the Good Faith Agreement sets forth a series of recommendations, including various levels of diversions and releases necessary during normal hydrological conditions and during periods of drought. The Good Faith Agreement was also followed during the 1985, 1989 and 2002 droughts.

For more information regarding litigation relating to the Water System, see “LITIGATION.”

## **The Sewer System**

The Sewer System is comprised of the sewage collection system and the water pollution control facilities. See “New York City Drainage Areas and Water Pollution Control Plants” map in Appendix H.

### *History*

Systematic collection of sewage and building of sewers began in the City as early as 1696. Major portions of the Sewer System in lower and central Manhattan were begun in the early 1830s and completed by 1870. The oldest sewer now in service was built in 1851. The oldest components of the Sewer System, located in Manhattan and Brooklyn, are constructed mostly of brick, clay and cement. The other Boroughs have newer sewers made primarily of vitreous clay and concrete. Historically, waste collection and disposal was a matter of local jurisdiction. Upon consolidation of the City in 1898, Presidents of the five Boroughs were given responsibility for sewage collection and disposal in their respective Boroughs. A Commissioner of Borough Works was established in each Borough for planning, constructing and administering its sewer system. This local responsibility for sewage collection existed until the mid-1960s.

Although water pollution control did not become a major issue until recent years, it has been a concern of local conservationists and public officials for over a century. The first water pollution control facility in the City was opened in 1886, when a small plant was constructed on Coney Island to protect the bathing beaches. In 1904, a Sanitary Commission was established and charged with developing a master plan for water pollution control in the City. Although the Sanitary Commission completed its task in 1910, water pollution control plant construction did not receive serious attention until 1929, when the City established a department to construct water pollution control facilities under the jurisdiction of the Department of Sanitation. In the 1930s this function was transferred to the Department of Public Works. In 1931, a plant construction program was begun to construct a system of water pollution control plants and associated facilities to control and treat all sewage produced within the City. The first of these plants, Coney Island, opened in 1935. Three larger plants, Wards Island, Tallmans Island and Bowery Bay, were placed in operation before the end of the 1930s. During the 1940s two additional plants, Jamaica and 26th Ward, were opened. The post-war years witnessed an intensified construction effort and, by 1967, 12 major treatment plants were in operation treating about 1,000 mgd at an average removal efficiency of about 65%. At that time most other urban areas were providing only about 35% removal efficiency.

The City Charter of 1963 consolidated the Borough sewer organizations into a City-wide department under the Department of Public Works. In 1968, various municipal services were consolidated into a single agency known as the Environmental Protection Administration, which included responsibility for sanitation and water and air quality resources. Within the Environmental Protection Administration, the Department of Water Resources had jurisdiction over the Bureaus of Water Supply and Water Pollution Control. These Bureaus were responsible for water supply and sewage collection and treatment. In 1977, water supply, sewage collection and treatment, and air quality monitoring responsibilities were combined into DEP.

### *Sewage Collection and Treatment*

The Sewer System's plants treat approximately 1,300 mgd of wastewater. The Sewer System is divided into 14 drainage areas corresponding to the 14 water pollution control plants and includes over 6,600 miles of sewer pipes of varying size which are classified as one of three types: sanitary, storm or combined. Sanitary sewers accommodate household and industrial waste. Storm sewers carry rainwater and surface water runoff. Combined sewers carry both types of waste. Approximately 70% of the City's sewers are of the combined type. In addition to the sewage pipes, the Sewer System includes catch basins and seepage basins to prevent flooding and sewer backups.

The Sewer System is comprised of a number of sewer facilities built to varying standards. Different materials and methods of construction were used resulting in different life cycles. Approximately 4,000

miles or two-thirds of the City’s sewer pipe is made of vitreous clay. Significant mileage of sewer pipe is composed of other building materials including cement, reinforced concrete, iron and brick. Some pipe in the collection system was installed before 1870, and approximately 15% of all sewer pipe in the collection system is over 100 years old.

The facilities related to the treatment of sewage include water pollution control plants, a combined sewer overflow treatment plant, wastewater pump stations, laboratories, sludge dewatering facilities and inner-harbor vessels which transport sludge between facilities. Sludge is a by-product of the sewage treatment process. Sludge that is treated through the sewage treatment process (or “biosolids”) is acceptable for land-based beneficial use.

Issues of both water supply volume and consequent sewage treatment volume are raised from time to time in connection with the System. Measures to increase the supply of water available to the System and to increase the sewage treatment capacity of the various water pollution control plants in the System are either being constructed under the CIP or are under continuing review for feasibility and cost effectiveness. However, the immediate approach to both the issues of supply and treatment capacity is conservation, through voluntary changes in user behavior, through education and the effect of actual use charges based on metered water usage, leak detection and repair and increased use of newly designed low-flow water use fixtures such as toilets.

The following table describes water pollution control plants currently in service.

**Water Pollution Control Facilities**

<u>Plants in Service</u>	<u>Capacity (mgd)</u>	<u>Year of Completion</u>	<u>Completion of Upgrading to Full Secondary Treatment or Reconstruction</u>
Newtown Creek.....	310	1967	2007
Wards Island.....	275	1937	1979
Hunts Point.....	200	1952	1978
Bowery Bay.....	150	1939	1978
Owls Head.....	120	1952	1995
Coney Island.....	110	1935	1994
Jamaica.....	100	1943	1978
26th Ward(1).....	85	1944	1979
Tallmans Island.....	80	1939	1978
Port Richmond.....	60	1953	1979
Rockaway.....	45	1952	1978
Oakwood Beach.....	40	1956	1979
North River.....	170	1986	1991
Red Hook.....	60	1987	1987
<u>Total System-wide Capacity.....</u>	<u>1,805</u>		

(1) There is a storm-overflow retention facility at Spring Creek, which is connected to the 26th Ward Plant.

The Sewer System’s water pollution control pump stations convey wastewater to the water pollution control plants. When gravity flow becomes uneconomical or not feasible for engineering reasons, pump stations lift the flow so that it can again flow by gravity. In some locations, pump stations utilize pressure piping called force mains to direct the flow of wastewater to the plants. The CIP includes an ongoing program to reconstruct and refurbish pump stations.

Sewer regulators and tide gates control flow in the System. Recent inspections of the regulator system have found it to be structurally adequate, but many portions are in need of mechanical reconstruction. A detailed evaluation of the regulator and tide gate system has been completed and funds have been provided in the CIP for mechanical refurbishment of these facilities.

During periods of heavy rainfall a combination of stormwater and sewage bypasses treatment and is released into the City’s waterways via combined sewer overflows. The combined sewer overflow abatement program provides for studies, design and construction of facilities to address this issue.

DEP has awarded contracts for the beneficial use of 100% of its biosolids which commenced in July 1998. These current contracts include: thermally drying the biosolids into fertilizer pellets at a facility

located in the Bronx; chemical reaction pelletization in Arkansas; direct land application in Colorado and Virginia; and lime stabilization in Colorado and New Jersey.

### *Governmental Regulation*

Under the Clean Water Act, USEPA oversees compliance with federal environmental laws, regulations and guidelines concerning sewage. Included in that regulatory framework is the National Pollutant Discharge Elimination System (“NPDES”) Permit Program and the issuance of water pollution control plant operating permits. As authorized by the Clean Water Act, administration of the permit program has been delegated to the State.

Pursuant to the Water Quality Act of 1987, as a condition for receipt of federal funds the State must establish a revolving fund to provide a source for loans to local entities for the construction of publicly-owned wastewater treatment facilities. Initial funding for a revolving fund program is provided from federal capitalization grants and state matching funds. The State has designated EFC to be the administrator of such funds.

*Full Secondary Treatment Requirements.* Thirteen of the System’s 14 in-City water pollution control plants have been upgraded to meet the full secondary treatment requirements of the Clean Water Act. The remaining plant, Newtown Creek, is in the process of being upgraded to meet federal requirements.

*SPDES.* On July 18, 2002, NYSDEC publicly noticed a proposal to modify the existing SPDES permits for the 14 in-City water pollution control plants operated and maintained by DEP. The SPDES permits for these facilities were issued in 1988 and, although administratively renewed from time to time, have not been significantly changed since such date. NYSDEC’s proposed modifications, if ultimately adopted, could increase costs for operating and maintaining the plants. On February 28, 2003, NYSDEC issued modified SPDES permits for all 14 plants. Although these permits address some of the concerns noted by DEP, the permits included effluent limits and requirements for nitrogen removal based on the 10 and 15 year target nitrogen waste load allocations set out in the Total Maximum Daily Load (“TMDL”) for dissolved oxygen in Long Island Sound (see “—Harbor and Waterway Protection”). Among other things, DEP objected to the inclusion of such limits and requirements because they were inconsistent with the limits and requirements of the Administrative Consent Order (as defined below) entered into with NYSDEC governing nitrogen discharges from the Upper East River water pollution control plant and because they would extend well beyond the 5-year life of the SPDES permits. DEP requested an adjudicatory hearing before an administrative law judge on the modified permits. After the parties submitted briefs addressing the inconsistencies between the permits and the Administrative Consent Order, the administrative law judge ruled in April 2004 that DEP has raised adjudicable issues. Currently, DEP and NYSDEC are attempting to negotiate a consensual resolution of this matter (see “—Harbor and Waterway Protection”). NYSDEC staff appealed that decision to the NYSDEC Commissioner, who appointed a representative to decide the issue. That appeal is pending.

The System includes eight City-owned upstate water pollution control plants to prevent untreated sewage from being released into the watersheds. To enhance watershed protection, DEP completed upgrades to seven of these facilities. The CIP includes funds to upgrade the eighth facility. DEP, through the City’s Law Department, takes legal action pursuant to the Clean Water Act to compel certain owners and operators of non-City owned water pollution control plants in the watersheds to comply with SPDES permits. In addition, DEP, together with the City Law Department, takes legal action to ensure that new developments are appropriately designed to be environmentally protective.

Over the past several years, NYSDEC and DEP have resolved various alleged permit violations at the System’s 14 in-City water pollution control plants by entering into “omnibus” consent orders. These administrative orders typically detail the alleged violations for a specified period of time and set forth remedial actions related to such violations. The most recent such consent order (the “Omnibus VI Consent Order”) covers alleged violations from January 1, 2000 through December 31, 2001, including alleged effluent, operating and bypass violations at a number of plants.

The City is also a party to litigation in which the court ordered the City to obtain a SPDES permit to operate the Shandaken Tunnel. On August 5, 2005, USEPA issued a memorandum, the conclusions of which support the City’s position with regard to the need for the City to obtain a SPDES permit to operate the Shandaken Tunnel. Based on this memorandum, the City is renewing its challenges to the need for a

SPDES permit for the operation of Shandaken Tunnel. See “LITIGATION.” On February 18, 2004, NYSDEC publicly noticed a draft SPDES permit for the Shandaken Tunnel which, among other items, contained provisions setting limits on flow, phosphorus, turbidity and temperature of water being discharged from the Shandaken Tunnel and requiring that the City take additional measures to reduce the amount of turbidity in water collected in the Schoharie Reservoir. In response to comments from DEP and others, NYSDEC withdrew the February draft permit. NYSDEC noticed a second draft permit for public comment on August 8, 2004. DEP requested an administrative hearing on the second draft permit. As with the first draft permit, the limits contained in the second draft would, in certain circumstances, impair the City’s ability to operate the Shandaken Tunnel, and the requirements for additional measures to reduce turbidity would involve substantial expenditures beyond those already included in the CIP. On June 22, 2005, the NYSDEC Administrative Law Judge overseeing the proceedings issued a decision identifying a number of issues as appropriate for adjudication. Hearings on these issues began on October 17, 2005.

*Combined Sewer Overflows.* The System is also required to develop programs to reduce pollution from combined sewer overflows and to eliminate excess infiltration and inflow into the Sewer System from ground and storm water. In June 1992, DEP entered into a consent order with the State (the “CSO Consent Order”) establishing various deadlines through 2006 for the construction of nine combined sewer overflow projects, which may include storage tanks. The CIP includes approximately \$685 million for such combined sewer overflow projects. Certain of the CSO Consent Order interim deadlines were not met, resulting in NYSDEC’s issuance of a notice of violation seeking monetary penalties. In December 2003, NYSDEC proposed revisions to the CSO Consent Order. After extended discussions, DEP and NYSDEC reached agreement on the terms of a revised CSO Consent Order, which was executed by DEP in August 2004 and by NYSDEC in January 2005. The revised CSO Consent Order provides for the payment of a \$4.5 million penalty for missed milestones under the original CSO Consent Order and establishes revised milestones for these projects which suffered delays. Certain of these milestones extend beyond the end of the CIP. The estimated additional cost of meeting these milestones is \$500 million. Consistent with USEPA guidelines, the City is exploring alternative approaches to combined sewer overflow problems that focus on cost-effective means of protecting water quality.

As noted above, DEP is participating in administrative proceedings with respect to the issuance, by NYSDEC, of modified SPDES permits for DEP’s 14 in-City water pollution control plants (see “—SPDES”). Each of these permits contains certain provisions relating to the control of combined sewer overflows. Prior to the execution of the revised CSO Consent Order, several environmental groups who are participating in the permit proceedings raised issues concerning the sufficiency of the City’s program to control such overflows. The Administrative Law Judge held these issues in abeyance and allowed NYSDEC and DEP an opportunity to discuss and reach agreement on potential modifications to the City’s program. This has been accomplished through the negotiation and execution of the revised CSO Consent Order and NYSDEC has advised the Judge that the revised Order has been finalized. Nonetheless, the parties who originally raised issues with respect to the City’s combined sewer overflow control program submitted supplemental petitions in the SPDES permit proceedings on April 4, 2005. Those petitions seek further changes in the CSO program and claim that the SPDES permits and revised order do not sufficiently address CSOs. An adjudication of these issues could result in additional permit provisions relating to the control of combined sewer overflows and/or a request to modify the terms of the revised CSO Consent Order.

*Harbor and Waterway Protection.* According to the most recent Harbor Survey issued by DEP, the water quality in New York Harbor and surrounding rivers continues to show long-term overall improvement. The Harbor Survey is an ongoing monitoring effort of the City’s waterways that has been done since 1909. The Survey monitors over a dozen water quality parameters at 37 sampling stations within New York Harbor and its tributaries. A key parameter of the overall health of aquatic systems is dissolved oxygen (“DO”). The Harbor Survey has found DO levels in most parts of the harbor at historic highs, although river-bottom DOs are periodically below acceptable concentrations. Over the past decade, compliance with New York State total and fecal coliform standards continues to be measured at the highest levels recorded by the Harbor Survey. Many local waterways, which were unfishable just 20 years ago, now meet the coliform bathing standards. The NYCDOH’s wet-weather advisories for most

public beaches (i.e. no swimming within 48 hours of a heavy rain) were lifted in June 1993. These water quality improvements are primarily a response to: continued water pollution control plant construction and upgrades; abatement and surveillance of illegal discharges; and increased capture of wet-weather flows.

In April 2004, the City health code for bathing beaches began utilizing a standard based on enterococcus, rather than coliform, which is regarded as a more precise indicator of water quality. DEP's Harbor Survey has begun a monitoring program for enterococcus and has been assisting the NYCDOH in its beach assessments.

As part of a cooperative effort to further improve water quality in the City's waterways, USEPA, along with the States of New York and New Jersey, recently released a Comprehensive Conservation Management Plan for the New York-New Jersey Harbor and the waters of the New York Bight. This Plan, developed under the aegis of the federal Harbor Estuary Program, builds on many of the City's ongoing programs such as water pollution control plant upgrades, controlling and capturing wet weather flows and reducing floatable debris. Under the Plan, the City will continue to promote improved water quality through, among other things, its efforts to eliminate combined sewer overflows, encourage water conservation, enhance surveillance of industrial discharges, and install sewers in areas of the City where they are not yet available. All of the capital commitments to be undertaken by the City pursuant to the Plan are already included in the CIP.

The Long Island Sound Study ("LISS") is a joint federal-state-local (the states being New York and Connecticut) program to identify the Long Island Sound's major environmental problems and develop a plan to manage those problems. USEPA is the lead federal agency involved in LISS. Hypoxia, or low levels of dissolved oxygen, has emerged as the issue of greatest concern in Long Island Sound. Hypoxia is the result of a chemical chain reaction that begins with high levels of nutrients, largely nitrogen. In addition to natural sources, other nutrient sources include effluent from water pollution control plants, stormwater run-off carrying lawn and agricultural fertilizer, organic materials, and air-deposited nitrate substances. As a result of the first and second phases of the LISS, the City agreed to limits in its SPDES permits for nitrogen discharges from its four Upper East River water pollution control plants. The construction required to meet these limits is complete and the City is meeting its current nitrogen discharge limits. In addition, the City has also entered into an Administrative Order on Consent with NYSDEC (the "Administrative Consent Order") which requires DEP to upgrade five water pollution control plants that discharge into the Upper East River or Jamaica Bay, respectively, to meet future more stringent nitrogen discharge limits. The CIP provides approximately \$2.5 billion for the upgrade of these five plants, including the implementation of a biological nutrient removal ("BNR") program to further reduce nitrogen levels in order to meet the Administrative Consent Order requirements. During construction, the Administrative Consent Order establishes less stringent nitrogen discharge limits than currently allowed by the City's SPDES permits for these plants. The TMDL was jointly prepared by the States of New York and Connecticut and approved by the USEPA in April 2001. The TMDL proposes the achievement of the dissolved oxygen standard in the Long Island Sound through the increased control of nitrogen from point sources, including certain of DEP's water pollution control plants, as well as through the control of other sources. DEP has proposed to NYSDEC and USEPA that the facility plan be modified to incorporate findings from the ongoing research to alleviate some over-conservatism in designs and make the program more cost-effective while still complying with nitrogen limits and construction deadlines specified in the Administrative Consent Order. DEP's revised program places greater emphasis on research findings, application of new technologies, and efficient management of resources. Early modeling results show that the revised program can provide an equal reduction in nitrogen levels to those anticipated by the original program. The independent Nitrogen Technical Advisory Committee, a blue ribbon panel of experts in the field, has endorsed the revised program (see "—SPDES").

By letter dated May 9, 2003, NYSDEC advised DEP that it had not agreed to any modification of the Administrative Consent Order, that DEP must comply with the provisions of the Administrative Consent Order as written, and that NYSDEC will enforce violations of the Administrative Consent Order, including the imposition of stipulated penalties. On March 12, 2004, NYSDEC issued a Notice of Violation to DEP alleging that DEP had violated certain milestones under the Administrative Consent



Order. Further, on March 25, 2004, NYSDEC issued a Determination rejecting DEP's revised facility plan. DEP and NYSDEC are attempting to negotiate a consensual resolution of this matter, which will impact the pending proceeding concerning SPDES permits for the 14 in-City water pollution control plants operated and maintained by DEP (see "—SPDES"). However, to protect the City's rights, on July 13, 2004, the City commenced an Article 78 proceeding against NYSDEC, challenging both the Notice of Violation and the Determination in the New York State Supreme Court, New York County. On April 8, 2005, the court found that NYSDEC did not abuse its discretion in rejecting DEP's revised facility plan, dismissed the City's petition and imposed penalties on the City. For further information, see "LITIGATION."

For more information on litigation relating to the Sewer System, see "LITIGATION."

## **ECONOMIC AND DEMOGRAPHIC INFORMATION**

This section presents information regarding certain economic and demographic information about the City. All information is presented on a calendar year basis unless otherwise indicated. The data set forth are the latest available. Sources of information are indicated in the text or immediately following the charts and tables. Although the Authority considers the sources to be reliable, the Authority has made no independent verification of the information provided by non-city sources and does not warrant its accuracy.

### **New York City Economy**

The City has a highly diversified economic base, with a substantial volume of business activity in the service, wholesale and retail trade and manufacturing industries, and is the location of many securities, banking, law, accounting, new media and advertising firms.

The City is a major seaport and focal point for international business. Many of the major corporations headquartered in the City are multinational in scope and have extensive foreign operations. Numerous foreign-owned companies in the United States are also headquartered in the City. These firms, which have increased substantially in number over the past decade, are found in all sectors of the City's economy, but are concentrated in trade, professional and business services, tourism and finance. The City is the location of the headquarters of the United Nations, and several affiliated organizations maintain their principal offices in the City. A large diplomatic community exists in the City to staff missions to the United Nations and the foreign consulates.

Economic activity in the City has experienced periods of growth and recession and can be expected to experience periods of growth and recession in the future. The City experienced a recession in the early 1970s through the middle of that decade, followed by a period of expansion in the late 1970s through the late 1980s. The City fell into recession again in the early 1990s which was followed by an expansion that lasted until 2001. The Financial Plan assumes that the economic slowdown that began in 2001 as a result of the September 11 attack, a national economic recession, and a downturn in the securities industry came to an end in 2004. The Financial Plan assumes continued moderate growth in calendar year 2005.

### **Personal Income**

Total personal income for City residents, unadjusted for the effects of inflation and the differential in living costs, increased from 1993 to 2002 (the most recent year for which City personal income data are available). From 1992 to 2002, personal income in the City averaged 4.3% growth compared to 5.1% for the nation. After increasing by 2.5% in 2003, total personal income is estimated by OMB to have increased in 2004. The following table sets forth information regarding personal income in the City from 1993 to 2003.

## Personal Income(1)

<u>Year</u>	<u>Total City (\$ billions)</u>	<u>Per Capita City</u>	<u>Per Capita U.S.</u>	<u>Per Capita City as a Percent of U.S.</u>
1993 .....	\$201.9	\$26,898	\$21,356	126.0%
1994 .....	207.5	27,403	22,176	123.6
1995 .....	221.2	28,981	23,078	125.6
1996 .....	234.1	30,407	24,176	125.8
1997 .....	245.5	31,579	25,334	124.7
1998 .....	262.0	33,341	26,880	124.0
1999 .....	275.4	34,658	27,933	124.1
2000.....	296.0	36,912	29,847	123.7
2001.....	302.7	37,520	30,572	122.7
2002.....	299.3	36,989	30,806	121.1
2003.....	306.7	37,815	31,476	120.1

Sources: U.S. Department of Commerce, Bureau of Economic Analysis and the Bureau of the Census Data as of March 15, 2005.

(1) In current dollars. Personal Income is based on the place of residence and is measured from income which includes wages and salaries, supplements to wages and salaries, proprietors' income, personal dividend income, personal interest income, rental income of persons and transfer payments.

### Employment Trends

The City is a leading center for the banking and securities industry, life insurance, communications, publishing, fashion design and retail fields. From 1989 to 1992, the City lost approximately 9% of its employment base. From 1993 to 2001, the City experienced significant private sector job growth with the addition of approximately 423,000 new private sector jobs (an average growth rate of approximately 2%). In 2002 and 2003, average annual employment in the City fell by approximately 108,600 and 51,800 jobs, respectively. In 2004, average annual employment in the City increased by 10,000 jobs. As of August 2005, total employment in the City was approximately 3,562,000 compared to approximately 3,521,900 in August 2004, an increase of approximately 1.1%.

The table below shows the distribution of employment from 1994 to 2004.

### Employment Distribution

	Average Annual Employment (in thousands)										
	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
<b>Goods Producing Sectors</b>											
Construction .....	88	90	91	93	101	112	120	122	116	113	111
Manufacturing .....	212	208	200	201	196	187	177	156	139	127	120
<b>Service Producing Sectors</b>											
Trade Transportation and Utilities .	526	533	533	538	542	556	570	557	536	534	538
Information .....	152	154	159	163	166	173	187	200	177	164	162
Financial Activities .....	472	467	464	468	477	481	489	474	445	434	435
Professional and Business Services .	437	445	468	494	525	553	587	582	550	537	537
Education and Health Services ....	536	552	565	576	589	606	620	627	646	658	667
Leisure and Hospitality .....	201	208	217	228	236	244	257	260	255	260	269
Other Services .....	121	123	125	129	134	142	147	149	150	149	150
<b>Total Private</b> .....	2,744	2,779	2,823	2,890	2,966	3,053	3,154	3,127	3,015	2,975	2,988
<b>Government</b> .....	578	560	546	552	561	567	569	565	569	557	554
<b>Total</b> .....	3,322	3,339	3,369	3,442	3,528	3,621	3,723	3,692	3,584	3,532	3,542

Note: Totals may not add due to rounding.

Source: U.S. Department of Labor, Bureau of Labor Statistics. Data are presented using the North American Industry Classification System ("NAICS").

### Sectoral Distribution of Employment and Earnings

In 2003, the City's service producing sectors provided approximately 2.8 million jobs and accounted for approximately 77% of total employment. Figures on the sectoral distribution of employment in the City from 1980 to 2000 reflect a significant shift to the service producing sectors and a shrinking manufacturing base relative to the nation.

The structural shift to the service producing sectors affects the total earnings as well as the average wage per employee because employee compensation in certain of those sectors, such as financial activities and professional and business services, tends to be considerably higher than in most other sectors. Moreover, average wage rates in these sectors are significantly higher in the City than in the nation. In the City in 2003, the employment share for the financial activities and professional and business services sectors was approximately 28% while the earnings share for that same sector was approximately 47%. In the nation, those same service producing sectors accounted for only approximately 18% of employment and 25% of earnings in 2003. Due to the earnings distribution in the City, sudden or large shocks in the financial markets may have a disproportionately adverse effect on the City relative to the nation.

The City's and the nation's employment and earnings by sector for 2003 are set forth in the following table.

**Sectoral Distribution of Employment and Earnings in 2003(1)**

	<u>Employment</u>		<u>Earnings(2)</u>	
	<u>NYC</u>	<u>U.S.</u>	<u>NYC</u>	<u>U.S.</u>
<b>Goods Producing Sectors</b>				
Mining . . . . .	0.0%	0.4%	0.3%	0.8%
Construction . . . . .	3.2	5.2	3.2	6.1
Manufacturing . . . . .	<u>3.6</u>	<u>11.2</u>	<u>2.7</u>	<u>13.5</u>
<b>Total Goods Producing</b> . . . . .	6.8	16.8	6.1	20.4
<b>Service Producing Sectors</b>				
Trade, Transportation and Utilities . . . . .	15.1	19.5	9.3	16.3
Information . . . . .	4.6	2.5	7.7	3.9
Financial Activities . . . . .	12.3	6.1	27.2	10.0
Professional and Business Services . . . . .	15.2	12.3	19.4	14.8
Education and Health Services . . . . .	18.6	12.8	11.1	10.8
Leisure & Hospitality . . . . .	7.4	9.4	3.8	3.9
Other Services . . . . .	<u>4.2</u>	<u>4.2</u>	<u>2.5</u>	<u>3.0</u>
<b>Total Service Producing</b> . . . . .	77.4	66.6	81.1	62.8
<b>Total Private Sector</b> . . . . .	84.2	83.4	88.8	83.5
<b>Government(3)</b> . . . . .	15.8	16.6	11.2	16.5

Note: Data may not add due to rounding or restrictions on reporting earnings data. Data are presented using NAICS. Sources: The two primary sources are the U.S. Department of Labor, Bureau of Labor Statistics and the U.S. Department of Commerce, Bureau of Economic Analysis.

- (1) The sectoral distributions are obtained by dividing each industry's employment or earnings by total non-agricultural employment or earnings.
- (2) Includes the sum of wage and salary disbursements, other labor income and proprietor's income. The latest information available is 2003 data.
- (3) Excludes military establishments.

The comparison of employment and earnings in 1980 and 2000 set forth below is presented using the industry classification system which was in use until the adoption of NAICS in the late 1990s. Though NAICS has been implemented for most government industry statistical reporting, most historical earnings data have not been converted. Furthermore, it is not possible to compare data from the two classification systems except in the general categorization of government, private and total employment. The table below reflects the overall increase in the service producing sectors and the declining manufacturing base in the City from 1980 to 2000.

The City's and the nation's employment and earnings by industry are set forth in the following table.

**Sectoral Distribution of Employment and Earnings(1)**

Sector	<u>Employment</u>				<u>Earnings(2)</u>			
	<u>1980</u>		<u>2000</u>		<u>1980</u>		<u>2000</u>	
	<u>NYC</u>	<u>U.S.</u>	<u>NYC</u>	<u>U.S.</u>	<u>NYC</u>	<u>U.S.</u>	<u>NYC</u>	<u>U.S.</u>
<b>Private Sector:</b>								
Non-Manufacturing:								
Services . . . . .	27.0%	19.8%	39.1%	30.7%	26.0%	18.4%	30.2%	28.7%
Wholesale and Retail Trade . . . . .	18.6	22.5	16.8	23.0	15.1	16.6	9.3	14.9
Finance, Insurance and Real Estate . . . . .	13.6	5.7	13.2	5.7	17.6	5.9	35.5	10.0
Transportation and Public Utilities . . . . .	7.8	5.7	5.7	5.3	10.1	7.6	5.2	6.8

Sector	Employment				Earnings(2)			
	1980		2000		1980		2000	
	NYC	U.S.	NYC	U.S.	NYC	U.S.	NYC	U.S.
Contract Construction . . . . .	2.3	4.8	3.3	5.1	2.6	6.3	2.9	5.9
Mining . . . . .	0.0	1.1	0.0	0.4	0.4	2.1	0.1	1.0
Total Non-Manufacturing . . . . .	69.3	59.6	78.1	70.3	71.8	56.9	83.2	67.3
Manufacturing:								
Durable. . . . .	4.4	13.4	1.6	8.4	3.7	15.9	1.3	10.5
Non-Durable. . . . .	10.6	9.0	4.9	5.6	9.5	8.9	4.8	6.1
Total Manufacturing . . . . .	15.0	22.4	6.5	14.0	13.2	24.8	6.1	16.6
<b>Total Private Sector . . . . .</b>	<b>84.3</b>	<b>82.0</b>	<b>84.7</b>	<b>84.3</b>	<b>85.2</b>	<b>82.1</b>	<b>89.8</b>	<b>84.6</b>
<b>Government(3) . . . . .</b>	<b>15.7</b>	<b>18.0</b>	<b>15.3</b>	<b>15.7</b>	<b>14.8</b>	<b>17.9</b>	<b>10.3</b>	<b>15.4</b>

Note: Totals may not add due to rounding. Data are presented using the Standard Industrial Classification System.  
Sources: The two primary sources of employment and earnings information are U.S. Department of Labor, Bureau of Labor Statistics, and U.S. Department of Commerce, Bureau of Economic Analysis.

- (1) The sectoral distributions are obtained by dividing each industry's employment or earnings by total non-agricultural employment or earnings.
- (2) Includes the sum of wage and salary disbursements, other labor income, and proprietors' income. The latest information available for the City is 2000 data.
- (3) Excludes military establishments.

## Population

The City has been the most populous city in the United States since 1790. The City's population is almost as large as the combined population of Los Angeles, Chicago and Houston, the three next most populous cities in the nation.

The following table provides information concerning the City's population.

### Population

Year	Population Total
1970 . . . . .	7,895,563
1980 . . . . .	7,071,639
1990 . . . . .	7,322,564
2000 . . . . .	8,008,278

Note: Figures do not include an undetermined number of undocumented aliens.

Source: U.S. Department of Commerce, Bureau of the Census.

## Housing

In 1999, the housing stock in the City consisted of approximately 3,039,000 housing units, excluding certain special types of units primarily in institutions such as hospitals and universities. The 1999 housing inventory represented an increase of approximately 44,000 units, or 1.5%, since 1996 and an increase of approximately 62,000 units, or 2.1% since 1993. The 1999 Housing and Vacancy Survey indicates that rental housing units predominate in the City. Of all occupied housing units in 1999, approximately 34% were conventional home-ownership units, cooperatives or condominiums and approximately 66% were rental units. In 2002, the housing stock in the City consisted of approximately 3,209,000 housing units. Due to the difference in the inventory basis for the draft 2002 Housing and Vacancy Survey and previous Housing and Vacancy Surveys, it is not possible to accurately compare 2002 results to the results of earlier Surveys until such time as the data is reweighted. The following table presents trends in the housing inventory in the City.

**Housing Inventory  
(In Thousands)**

<u>Ownership/Occupancy Status</u>	<u>1981</u>	<u>1984</u>	<u>1987</u>	<u>1991</u>	<u>1993</u>	<u>1996</u>	<u>1999</u>	<u>2002</u>
Total Housing Units . . . . .	2,792	2,803	2,840	2,981	2,977	2,995	3,039	3,209
Owner Units . . . . .	755	807	837	858	825	858	932	997
Owner-Occupied . . . . .	746	795	817	829	805	834	915	982
Vacant for Sale . . . . .	9	12	19	29	20	24	17	15
Rental Units . . . . .	1,976	1,940	1,932	2,028	2,040	2,027	2,018	2,085
Renter-Occupied . . . . .	1,934	1,901	1,884	1,952	1,970	1,946	1,953	2,024
Vacant for Rent . . . . .	42	40	47	77	70	81	64	61
Vacant Not Available for Sale or Rent(1) . . . . .	62	56	72	94	111	110	89	127

Note: Details may not add up to totals due to rounding.

Sources: U.S. Bureau of the Census, 1981, 1984, 1987, 1991, 1993, 1996, 1999 and draft 2002 New York City Housing and Vacancy Surveys.

(1) Vacant units that are dilapidated, intended for seasonal use, held for occasional use, held for maintenance purposes or other reasons.

**LITIGATION**

There is no action, suit, proceeding or investigation, at law or in equity, before or by any court, public board or body pending or, to the best knowledge of the Authority, threatened against or affecting the Authority to restrain or enjoin the issuance, sale or delivery of the Fiscal 2006 AA Bonds or in any way contesting or affecting the validity of the Fiscal 2006 AA Bonds or any proceedings of the Authority, the Board or the City taken with respect to the issuance or sale of the Fiscal 2006 AA Bonds or with respect to the Second Resolution or the pledge or application of any money or security provided for the payment of the Fiscal 2006 AA Bonds or the existence or powers of the Authority or the Board.

Pursuant to the Lease and the Agreement, the City has agreed, subject to certain conditions, to indemnify the Authority and the Board against any and all liability in connection with any act done or omitted in the exercise of their powers which is taken or omitted in good faith in pursuance of their purposes under the Act. The City, however, is entitled to reimbursement by the Board for the amount of any judgment or settlement paid by the City (and not otherwise reimbursed from any other source) arising out of a tort or contract claim to the extent that the City's liability therefor is related to the operation, maintenance and improvement of the System provided, however, that the Board is not required to reimburse the City in any one year for tort claims in excess of 5% of the Revenues of the Board for such Fiscal Year.

There are numerous claims seeking damages and injunctive and other relief against the City related to the System. Except as noted below, these claims represent routine litigation incidental to the performance of the City's governmental functions in connection with the operation, maintenance and improvement of the System. The City has paid an average of approximately \$5.3 million per year from Fiscal Years 1995 through 2004 in satisfaction of tort claims relating to the operation of the System. Approximately \$3.5 million of such claims allege property damage and approximately \$1.8 million of these claims allege personal injury. Contract claims on water supply, sewer and water pollution control projects arise in varying amounts based on alleged change orders and related matters. While most seek under \$10 million in damages, one action seeks damages of approximately \$32 million. While the probable outcome of these actions cannot be determined at this time, contract claims are expected to be funded through the CIP, which may be revised from time to time to accommodate such claims as well as other changes therein. The ultimate outcome of the proceedings described below is not currently predictable, and unfavorable determinations therein could result in substantial expenditures.

In March 2000, several fishing and sporting groups filed a lawsuit against the City and DEP in the United States District Court for the Northern District of New York, claiming that DEP's operation of the Shandaken Tunnel violated the Clean Water Act. Because water discharged from the tunnel into the Esopus Creek is frequently turbid, plaintiffs alleged that the discharge of turbid water amounts to the

addition of a pollutant to the creek from a point source, requiring a SPDES permit. Although the City's motion to dismiss was granted in October 2000 by the District Court, on October 23, 2001 the Second Circuit reversed and held that the Clean Water Act requires SPDES permits for discharges caused when one water body is artificially diverted into a second water body. In late May 2002, the District Court granted the plaintiffs' motion for summary judgment on the issue of liability. In February 2003, after a bench trial on the issues of remedies and penalties, the District Court determined that it was reasonable for the City to believe that a SPDES permit was not required for the operation of the Shandaken Tunnel prior to the Second Circuit decision in October 2001. The Court also determined that given the need to secure the safety of the System after the events of September 11, 2001, the City's delay in filing an application for a SPDES permit until December 2002 did not evidence a lack of good faith. Nonetheless, the Court imposed approximately \$5.7 million in statutory penalties on the City for operating the Shandaken Tunnel without a SPDES permit from June 22, 2002 to December 30, 2002, the date of the City's application for a SPDES permit. Apart from directing the City to pursue the permit, the Court ordered no specific remedy. The City filed a notice of appeal indicating its appeal of the District Court decision to the United States Court of Appeals for the Second Circuit. The appeal is pending. On August 5, 2005, USEPA issued an interpretation of the Clean Water Act, in which it concluded that NPDES/SPDES permits are not required for water transfers, such as the City's transfer of water through the Shandaken Tunnel. On August 15, 2005, the City filed a motion to submit a supplemental brief to the Second Circuit and attached a proposed supplemental brief discussing the USEPA interpretation. The Second Circuit has not yet ruled on the City's motion. On August 30, 2005, the City filed a motion with the District Court for a stay of its February 2003 Order, to the extent that it requires NYSDEC to make a determination on the City's application for a SPDES permit for the Shandaken Tunnel within eighteen months of the Court's order, and an order enjoining NYSDEC from proceeding with the City's application. Opposition briefs were submitted on September 9, 2005. As of October 17, 2005, the Court had not yet ruled on the City's motion.

Simultaneously with such litigation, NYSDEC has continued negotiation with DEP for a SPDES permit for the Shandaken Tunnel. On February 18, 2004, NYSDEC publicly noticed a draft SPDES permit for the Shandaken Tunnel which, in response to comments from DEP and others, NYSDEC subsequently withdrew. NYSDEC noticed a second draft permit for public comment on August 8, 2004. DEP requested an administrative hearing on the second draft permit. As with the first draft permit, the limits contained in the second draft would, in certain circumstances, impair the City's ability to operate the Shandaken Tunnel, and the requirements for additional measures to reduce turbidity would involve substantial expenditures beyond those already included in the CIP. On June 22, 2005, the NYSDEC Administrative Law Judge overseeing the administrative hearing issued a decision identifying a number of issues as appropriate for adjudication. Hearings on these issues began on October 17, 2005. For additional information on SPDES permits, see "THE SYSTEM—The Sewer System—Governmental Regulation—SPDES."

Four actions have been commenced seeking to enjoin construction of the Croton filtration plant at the Mosholu Golf Course site, alleging that DEP's environmental review was inadequate and that the site was not appropriately zoned as a water treatment plant. In all the actions, the trial court has dismissed the petitions. The petitioners in one action have appealed the dismissals. In a second action, the intermediate appellate court upheld the dismissal and petitioners have sought permission to appeal to the highest state appeals court. The City has opposed that request. The petitioners' time to appeal on the remaining two actions has passed and those actions are now concluded. Therefore, DEP is free to continue work on the site, which began in late 2004. The City believes its position is meritorious in these actions and intends to defend them vigorously.

A counterclaim has been brought against the City in connection with DEP's proposal to NYSDEC and USEPA to modify the Administrative Consent Order with respect to the management of hypoxia in the Long Island Sound. The City had brought an Article 78 proceeding against NYSDEC in New York Supreme Court, New York County, on July 13, 2004, challenging certain determinations made by NYSDEC in connection with DEP's proposal. NYSDEC brought a counterclaim to this proceeding and on April 8, 2005, the court found that NYSDEC did not abuse its discretion in rejecting DEP's revised

facility plan and dismissed the City's petition. The court further found that NYSDEC is entitled to penalties under the Administrative Consent Order in the amount of \$13.116 million, to be deposited in an escrow account and released to the City if DEP complies with the final construction milestones in the Administrative Consent Order. The City took an appeal, thereby invoking an automatic stay of the April 18, 2005 court order. Because DEP remains in non-compliance with the Administrative Consent Order, the penalties will increase over time. If DEP were required to proceed with the construction called for in the original facility plan approved by NYSDEC, DEP does not believe it could comply with the construction milestones in the Administrative Consent Order and believes that the cost of such construction would exceed the amount currently provided in the CIP by approximately \$900 million. The City is negotiating a resolution of this matter with NYSDEC. For more information on the Administrative Consent Order and the plan to manage hypoxia in the Long Island Sound, see "THE SYSTEM—The Sewer System—Governmental Regulation—Harbor and Waterway Protection."

### **APPROVAL OF LEGAL PROCEEDINGS**

The issuance of the Fiscal 2006 AA Bonds is subject to the approval of legality by Orrick, Herrington & Sutcliffe LLP, New York, New York, Bond Counsel. Certain legal matters will be passed upon for the City and the Board by the City's Corporation Counsel. Certain legal matters will be passed upon for the Underwriters by Nixon Peabody LLP, New York, New York. Certain legal matters will be passed upon for State Street Bank and Trust Company by King & Spalding LLP. Certain legal matters will be passed upon for California State Teachers' Retirement System by Fulbright & Jaworski L.L.P. Certain legal matters will be passed upon for Dexia Crédit Local, acting through its New York Branch, by King & Spalding LLP and by Jeantet & Associates.

### **FINANCIAL ADVISORS**

Lamont Financial Services Corporation and Ramirez & Co., Inc. have served as financial advisors to the Authority with respect to the sale of the Fiscal 2006 AA Bonds.

### **FURTHER INFORMATION**

The references herein to and summaries of federal, State and local laws, including but not limited to the Code, the Constitution and laws of the State, the Act, the 1905 Act, the Clean Water Act, the SDWA, the Ban Act, the MPRSA, and documents, agreements and court decisions, including but not limited to the Lease, the Agreement, the Second Resolution and the First Resolution are summaries of certain provisions thereof. Such summaries do not purport to be complete and are qualified in their entirety by reference to such acts, laws, documents, agreements or decisions. Copies of the Lease, the Agreement, the Second Resolution and the First Resolution are available for inspection during normal business hours at the office of the Authority.

Any statements in this Official Statement involving matters of opinion, whether or not expressly so stated, are intended as such and not as representations of fact. Neither this Official Statement nor any statement which may have been made orally or in writing shall be construed as a contract or as a part of a contract with the original purchasers or any holders of the Fiscal 2006 AA Bonds.

### **CONTINUING DISCLOSURE UNDER SEC RULE 15c2-12**

For so long as the Fiscal 2006 AA Bonds bear interest in a Rate Period other than the Initial Rate Period, a Daily Rate Period, a Weekly Rate Period or a Commercial Rate Period of 270 days or less, and to the extent that Rule 15c2-12 (the "Rule") of the Securities and Exchange Commission ("SEC") under the Securities and Exchange Act of 1934, as amended (the "1934 Act"), requires the respective Underwriters to determine, as a condition to purchasing the Fiscal 2006 AA Bonds, that the Authority will covenant to the effect of the provisions here summarized (the "Undertaking"), and the Rule as so applied is authorized by a federal law that as so construed is within the powers of Congress, the Authority agrees with the record and beneficial owners from time to time of the Fiscal 2006 AA Bonds ("Bondholders") that it will:



(1) within 240 days after the end of each Fiscal Year, deliver to each nationally recognized municipal securities information repository and to any New York State information depository, core financial information and operating data for the prior Fiscal Year, including (i) the System's audited financial statements, prepared in accordance with generally accepted accounting principles in effect from time to time, and (ii) material historical financial and operating data concerning the System and the Revenues of the System generally of the type included in this Official Statement under the captions "CAPITAL IMPROVEMENT AND FINANCING PROGRAM," "FINANCIAL OPERATIONS," "RATES AND BILLING" and "THE SYSTEM;"

(2) provide in a timely manner, to each nationally recognized municipal securities information repository or to the Municipal Securities Rulemaking Board, and to any New York State information depository, notice of any of the following events with respect to the Fiscal 2006 AA Bonds, if material:

(a) principal and interest payment delinquencies;

(b) non-payment related defaults;

(c) in the case of credit enhancement that is provided in connection with the issuance of the Fiscal 2006 AA Bonds, unscheduled draws on such credit enhancement reflecting financial difficulties and substitution of credit providers, or their failure to perform;

(d) unscheduled draws on debt service reserves reflecting financial difficulties;

(e) adverse opinions or events affecting the exclusion from gross income for federal income tax purposes of interest on the Fiscal 2006 AA Bonds;

(f) modifications to rights of security holders;

(g) bond calls;

(h) defeasances;

(i) release, substitution, or sale of property securing repayment of the securities;

(j) rating changes; and

(3) provide in a timely manner, to each nationally recognized municipal securities information repository or to the Municipal Securities Rulemaking Board, and to any New York State information depository, notice of any failure by the Authority to comply with clause (1), above.

The Authority expects to provide the information described in clause (1) above by delivering its first bond official statement that includes its financial statements for the preceding fiscal year.

Currently, there is no New York State information depository and the nationally recognized municipal securities information repositories are: Bloomberg Municipal Repository, 100 Business Park Drive, Skillman, New Jersey 08558; Standard & Poor's J.J. Kenny Repository, 55 Water Street, 45th Floor, New York, New York 10041; FT Interactive Data, 100 William Street, New York, NY 10038, Attn: NRMSIR and DPC Data Inc., One Executive Drive, Fort Lee, New Jersey 07024.

No Bondholder may institute any suit, action or proceeding at law or in equity ("Proceeding") for the enforcement of the Undertaking or for any remedy for breach thereof, unless such Bondholder has filed with the Authority evidence of ownership and a written notice of and request to cure such breach, and the Authority has not complied within a reasonable time; provided, however, that any Proceeding challenging the adequacy of any information provided pursuant to paragraphs (1) and (2) above may be brought only by the Trustee or the holders of a majority in aggregate principal amount of the Fiscal 2006 AA Bonds affected thereby which at the time are Outstanding. All Proceedings may be instituted only as specified herein, in the federal or State courts located in the Borough of Manhattan, State and City of New York, and for the equal benefit of all holders of the Outstanding Bonds benefited by the same or a substantially similar covenant. No remedy may be sought or granted other than specific performance of the covenant at issue.

Any amendment to the Undertaking will take effect only if:

(a) the amendment is made in connection with a change in circumstances that arises from a change in legal requirements, change in law, or change in the identity, nature, or status of the Authority or the Board, or type of business conducted; the Undertaking, as amended, would have complied with the requirements of the Rule at the time of sale of the Fiscal 2006 AA Bonds to the Underwriters, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances; and the amendment does not materially impair the interests of Bondholders, as determined by parties unaffiliated with the Authority (such as, but without limitation, the Authority's financial advisor or bond counsel) and the annual financial information containing (if applicable) the amended operating data or financial information will explain, in narrative form, the reasons for the amendment and the "impact" (as that word is used in the letter from the staff of the SEC to the National Association of Bond Lawyers dated June 23, 1995) of the change in the type of operating data or financial information being provided; or

(b) all or any part of the Rule, as interpreted by the staff of the SEC at the date of the Undertaking, ceases to be in effect for any reason, and the Authority elects that the Undertaking will be deemed terminated or amended (as the case may be) accordingly.

For purposes of the Undertaking, a beneficial owner of a security includes any person who, directly or indirectly, through any contract, arrangement, understanding, relationship, or otherwise has or shares investment power which includes the power to dispose, or to direct the disposition of, such security, subject to certain exceptions, as set forth in the Undertaking. Any assertion of beneficial ownership must be filed, with full documentary support, as part of the written request to the Authority described above.

## **INVESTMENTS**

The Authority invests moneys available in the Debt Service Fund, Construction Fund and the Revenue Fund. Investments are made pursuant to restrictions contained in the Resolutions and the Authority's Investment Guidelines as adopted and modified from time to time by the Authority's Board of Directors. In conjunction with the annual audit of the financial statements of the System, the independent auditors are required to provide to the Authority's Board of Directors an Investment Compliance letter confirming compliance with both the Authority's Investment Guidelines and with Investment Guidelines of Public Authorities of the State Comptroller of New York. Annual valuation of all funds is at the lower of amortized cost or market value. For other investment restrictions, see "APPENDIX C—GLOSSARY AND SUMMARY OF CERTAIN DOCUMENTS." The Authority's primary objective in investment of its available funds is preservation of principal. The Authority is not legally authorized to enter into reverse repurchase agreements. The Authority does not make leveraged investments.

## **RATINGS**

The Authority has applied for long-term and short-term ratings for the Fiscal 2006 AA Bonds from S&P, Moody's and Fitch.

Such ratings will reflect only the views of the respective rating agencies, from which an explanation of the significance of such ratings may be obtained. There is no assurance that any rating will continue for any given period of time or that any or all will not be revised downward or withdrawn entirely. Any such downward revision or withdrawal could have an adverse effect on the market price of the Fiscal 2006 AA Bonds.

## **UNDERWRITING**

Goldman, Sachs & Co. has agreed, subject to certain conditions, to purchase the Fiscal 2006 AA-1 Bonds from the Authority at an aggregate price of \$199,988,000.00. Banc of America Securities LLC has agreed, subject to certain conditions, to purchase the Fiscal 2006 AA-2 Bonds from the Authority at an aggregate price of \$99,994,000.00. Loop Capital Markets, LLC has agreed, subject to certain conditions, to purchase the Fiscal AA-3 Bonds from the Authority at an aggregate price of \$99,994,000.00. The

obligations of each of the Underwriters are subject to certain conditions precedent, and each of the Underwriters will be obligated to purchase all of the respective Sub-Series of Fiscal 2006 AA Bonds if any of the respective Sub-Series of Fiscal 2006 AA Bonds are purchased. The Fiscal 2006 AA Bonds may be offered and sold to certain dealers (including the Underwriters and other dealers depositing the Fiscal 2006 AA Bonds into investment trusts) and others at prices lower than such public offering price and such public offering price may be changed, from time to time, by the Underwriters.

### **LEGALITY FOR INVESTMENT AND DEPOSIT**

Under the Act, the Fiscal 2006 AA Bonds are securities in which all public officials and bodies of the State and all municipalities, all insurance companies and associations and other persons carrying on an insurance business, all banks, bankers, trust companies, savings banks and savings associations, including savings and loan associations, investment companies and other persons carrying on a banking business, and administrators, guardians, executors, trustees and other fiduciaries and all others persons whatsoever, who are now and may hereafter be authorized to invest in the Fiscal 2006 AA Bonds or obligations of the State, may properly and legally invest funds including capital in their control or belonging to them in such Fiscal 2006 AA Bonds. The Act further provides that the Fiscal 2006 AA Bonds are securities which may be deposited with and may be received by all public officers and bodies of the State and all municipalities for any purposes for which the deposit of bonds or other obligations of the State is or may hereafter be authorized.

### **FINANCIAL STATEMENTS AND INDEPENDENT AUDITORS**

The financial statements of the System as of and for the year ended June 30, 2004 (the “Audited System Financial Statements”) included in Appendix D to this Official Statement have been audited by Grant Thornton LLP, independent auditors, as stated in their report appearing therein.

### **ENGINEERING FEASIBILITY REPORT AND FORECASTED CASH FLOWS**

Certain information contained in this Official Statement under the captions “CAPITAL IMPROVEMENT AND FINANCING PROGRAM—Capital Improvement Program,” “THE SYSTEM—The Water System,” “THE SYSTEM—The Sewer System” has been reviewed and independently evaluated by Metcalf & Eddy which has provided the opinion letter set forth in Appendix A confirming such information. Metcalf & Eddy also serves as a consulting engineer to DEP on capital projects relating to the System. As a result of occasional, routine litigation initiated by third parties arising from such projects, Metcalf & Eddy and the City have from time to time been either co-parties or adverse parties in such litigation.

Certain financial forecasts contained in this Official Statement in the tables titled “Sources and Uses of Capital Funds” and “Future Debt Service Requirements” under the caption “CAPITAL IMPROVEMENT AND FINANCING PROGRAM” and “Projected Operating and Maintenance Expenses,” “Projected Revenues,” and “Forecasted Cash Flows” under the caption “FINANCIAL OPERATIONS” have been examined by Amawalk Consulting, to the extent and for the periods indicated in those tables. The conclusions of Amawalk Consulting with respect to the reasonableness of the forecasts are set forth in an opinion letter attached hereto as Appendix B. The President of Amawalk Consulting has provided consulting services including feasibility studies, rate studies and organizational analysis to numerous clients in the water and wastewater industry including the City of New York Water and Sewer System, the Boston Water and Sewer Commission and the Shanghai, PRC Water and Sewer.

### **TAX MATTERS**

In the opinion of Orrick, Herrington & Sutcliffe LLP (“Bond Counsel”), based upon an analysis of existing laws, regulations, rulings and court decisions, and assuming, among other matters, the accuracy of certain representations and compliance with certain covenants, interest on the Fiscal 2006 AA Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986 (the “Code”). Bond Counsel is of the further opinion that interest on the Fiscal 2006 AA Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although Bond Counsel observes that such interest is included in adjusted current earnings when calculating corporate alternative minimum taxable income. Bond Counsel is also of the

opinion that interest on the Fiscal 2006 AA Bonds is exempt from personal income taxes imposed by the State of New York and any political subdivision thereof (including The City of New York). A complete copy of the proposed form of opinion of Bond Counsel is set forth in Appendix E hereto.

To the extent the issue price of any maturity of the Fiscal 2006 AA Bonds is less than the amount to be paid at maturity of such Fiscal 2006 AA Bonds (excluding amounts stated to be interest and payable at least annually over the term of such Fiscal 2006 AA Bonds), the difference constitutes “original issue discount,” the accrual of which, to the extent properly allocable to each Beneficial Owner thereof, is treated as interest on the Fiscal 2006 AA Bonds which is excluded from gross income for federal income tax purposes. For this purpose, the issue price of a particular maturity of the Fiscal 2006 AA Bonds is the first price at which a substantial amount of such maturity of the Fiscal 2006 AA Bonds is sold to the public (excluding bond houses, brokers, or similar persons or organizations acting in the capacity of underwriters, placement agents or wholesalers). The original issue discount with respect to any maturity of the Fiscal 2006 AA Bonds accrues daily over the term to maturity of such Fiscal 2006 AA Bonds on the basis of a constant interest rate compounded semiannually (with straight-line interpolations between compounding dates). The accruing original issue discount is added to the adjusted basis of such Fiscal 2006 AA Bonds to determine taxable gain or loss upon disposition (including sale, redemption, or payment on maturity) of such Fiscal 2006 AA Bonds. Beneficial Owners of the Fiscal 2006 AA Bonds should consult their own tax advisors with respect to the tax consequences of ownership of Fiscal 2006 AA Bonds with original issue discount, including the treatment of Beneficial Owners who do not purchase such Fiscal 2006 AA Bonds in the original offering to the public at the first price at which a substantial amount of such Fiscal 2006 AA Bonds is sold to the public.

Fiscal 2006 AA Bonds purchased, whether at original issuance or otherwise, for an amount higher than their principal amount payable at maturity (or, in some cases, at their earlier call date) (“Premium Bonds”) will be treated as having amortizable bond premium. No deduction is allowable for the amortizable bond premium in the case of bonds, like the Premium Bonds, the interest on which is excluded from gross income for federal income tax purposes. However, the amount of tax-exempt interest received, and a Beneficial Owner’s basis in a Premium Bond, will be reduced by the amount of amortizable bond premium properly allocable to such Beneficial Owner. Beneficial Owners of Premium Bonds should consult their own tax advisors with respect to the proper treatment of amortizable bond premium in their particular circumstances.

The Code imposes various restrictions, conditions and requirements relating to the exclusion from gross income for federal income tax purposes of interest on obligations such as the Fiscal 2006 AA Bonds. The Authority has made certain representations and covenanted to comply with certain restrictions, conditions and requirements designed to ensure that interest on the Fiscal 2006 AA Bonds will not be included in federal gross income. Inaccuracy of these representations or failure to comply with these covenants may result in interest on the Fiscal 2006 AA Bonds being included in gross income for federal income tax purposes, possibly from the date of original issuance of the Fiscal 2006 AA Bonds. The opinion of Bond Counsel assumes the accuracy of these representations and compliance with these covenants. Bond Counsel has not undertaken to determine (or to inform any person) whether any actions taken (or not taken), or events occurring (or not occurring), or any other matters coming to Bond Counsel’s attention after the date of issuance of the Fiscal 2006 AA Bonds may adversely affect the value of, or the tax status of interest on, the Fiscal 2006 AA Bonds.

Certain requirements and procedures contained or referred to in the Second Resolution, the Agreement, the Tax Certificate and Agreement, and other relevant documents may be changed and certain actions (including, without limitation, defeasance of the Fiscal 2006 AA Bonds) may be taken or omitted under the circumstances and subject to the terms and conditions set forth in such documents. Bond Counsel expresses no opinion as to any Fiscal 2006 AA Bond or the interest thereon if any such change occurs or action is taken or omitted upon the advice or approval of bond counsel other than Orrick, Herrington & Sutcliffe LLP.

Although Bond Counsel is of the opinion that interest on the Fiscal 2006 AA Bonds is excluded from gross income for federal income tax purposes and is exempt from personal income taxes imposed by the

State of New York and any political subdivision thereof (including The City of New York), the ownership or disposition of, or the accrual or receipt of interest on, the Fiscal 2006 AA Bonds may otherwise affect a Beneficial Owner's federal, state or local tax liability. The nature and extent of these other tax consequences depends upon the particular tax status of the Beneficial Owner or the Beneficial Owner's other items of income or deduction. Bond Counsel expresses no opinion regarding any such other tax consequences.

Future legislation, if enacted into law, or clarification of the Code may cause interest on the Fiscal 2006 AA Bonds to be subject, directly or indirectly, to federal income taxation, or otherwise prevent Beneficial Owners from realizing the full current benefit of the tax status of such interest. The introduction or enactment of any such future legislation or clarification of the Code may also affect the market price for, or marketability of, the Fiscal 2006 AA Bonds. Prospective purchasers of the Fiscal 2006 AA Bonds should consult their own tax advisers regarding any pending or proposed federal tax legislation, as to which Bond Counsel expresses no opinion.

The opinion of Bond Counsel is based on current legal authority, covers certain matters not directly addressed by such authorities, and represents Bond Counsel's judgment as to the proper treatment of the Fiscal 2006 AA Bonds for federal income tax purposes. It is not binding on the Internal Revenue Service ("IRS") or the courts. Furthermore, Bond Counsel cannot give and has not given any opinion or assurance about the future activities of the Authority, or about the effect of future changes in the Code, the applicable regulations, the interpretation thereof or the enforcement thereof by the IRS. The Authority has covenanted, however, to comply with the requirements of the Code.

Bond Counsel's engagement with respect to the Fiscal 2006 AA Bonds ends with the issuance of the Fiscal 2006 AA Bonds, and, unless separately engaged, Bond Counsel is not obligated to defend the Authority or the Beneficial Owners regarding the tax-exempt status of the Fiscal 2006 AA Bonds in the event of an audit examination by the IRS. Under current procedures, parties other than the Authority and its appointed counsel, including the Beneficial Owners, would have little, if any, right to participate in the audit examination process. Moreover, because achieving judicial review in connection with an audit examination of tax-exempt bonds is difficult, obtaining an independent review of IRS positions with which the Authority legitimately disagrees, may not be practicable. Any action of the IRS, including but not limited to selection of the Fiscal 2006 AA Bonds for audit, or the course or result of such audit, or an audit of bonds presenting similar tax issues may affect the market price for, or the marketability of, the Fiscal 2006 AA Bonds, and may cause the Authority or the Beneficial Owners to incur significant expense.

#### **CERTAIN LEGAL OPINIONS**

At the request of the Authority, Bond Counsel reviewed issues related to the effects on the Board and the Authority of a case under Title 11 of the United States Bankruptcy Code (the "Bankruptcy Code") in which the City is a debtor. Specifically, Bond Counsel considered whether a court, exercising reasonable judgment after full consideration of all relevant factors, would (i) hold that the Revenues derived from operation of the System would be property of the bankruptcy estate of the City, (ii) hold that the rights of the Board to the Revenues and the interest of the Authority in the Revenues would be subject to a stay, by operation of Section 922(a) of the Bankruptcy Code or (iii) order the substantive consolidation of the assets of either or both the Board and the Authority with those of the City. Based upon its review of the Act, the Lease, the Agreement, the First Resolution, the Second Resolution and such other matters of law and fact as it considered relevant, and recognizing that there is no definitive judicial authority confirming the correctness of its analysis, Bond Counsel has rendered to the Authority its opinion, subject to all the facts, assumptions and qualifications set forth therein, that under the Bankruptcy Code a court, in the circumstances described above, (i) would not hold that the Revenues would be property of the City or that the Board's right to and the Authority's interest in the Revenues would be subject to a stay by operation of Section 922(a) of the Bankruptcy Code, and (ii) would not order the substantive consolidation of the assets and liabilities of either the Board or the Authority with those of the City. This opinion will be based on an analysis of existing laws, regulations, rulings and court decisions, and will cover certain matters not directly addressed by such authorities. There are no court decisions directly on point.

Bond Counsel is also of the opinion that, subject to all the facts, assumptions and qualifications set forth therein, in a case under the Bankruptcy Code in which the City is a debtor (i) should the City elect to assume the Lease, the Lease would continue pursuant to its terms and (ii) should the City elect to reject the Lease, the Board may elect to retain its rights under the Lease and remain in possession and enjoy the use of the System and the right to the Revenues derived therefrom for the unexpired balance of the term of the Lease.

The Bankruptcy Code provides that in order for a municipality to be a Chapter 9 debtor it must be specifically authorized by State law to be a debtor under Chapter 9 of the Bankruptcy Code. Bond Counsel is of the opinion, subject to all the facts, assumptions and qualifications set forth therein, that under the Bankruptcy Code neither the Authority nor the Board could properly be a debtor in a voluntary or involuntary case under the Bankruptcy Code.

Bond Counsel has not rendered an opinion, however, as to any preliminary or temporary stay, injunction or order which a bankruptcy court might issue pursuant to its powers under 11 U.S.C. §§ 105 or 362 to preserve the status quo pending consideration of the substantive legal issues discussed above. Moreover, the opinions expressed above have inherent limitations because of the pervasive equity powers of bankruptcy courts as they relate to the business and creditor relationships leading up to the bankruptcy as well as generally the overriding goal of reorganization to which other legal rights and policies may be subordinated, the potential relevance to the exercise of judicial discretion of future-arising facts and circumstances, and the nature of the bankruptcy process; and are based on an analysis of existing laws, regulations, rulings and court decisions. Such opinions may be adversely affected by actions taken or events occurring, including a change in law, regulation or ruling (or in the application or official interpretation of any law, regulation or ruling) after the date of this Official Statement. Bond Counsel has not undertaken to determine, or to inform any person, whether such actions are taken or such events occur and has no obligation to update this section in light of such actions or events.

NEW YORK CITY MUNICIPAL WATER  
FINANCE AUTHORITY

**LETTER OF  
METCALF & EDDY OF NEW YORK, INC.,  
CONSULTING ENGINEERS**

October 18, 2005

Mr. Alan L. Anders  
Executive Director  
New York City Municipal Water Finance Authority

Subject: New York City Municipal Water Finance Authority  
Water and Sewer System Second General Resolution Revenue Bonds,  
Fiscal 2006 Series AA

Dear Mr. Anders:

We hereby submit the opinion of Metcalf & Eddy of New York, Inc. (“Metcalf & Eddy”) on the Engineering Feasibility of the Water and Sewer System serving The City of New York (the “City”). Capitalized terms used herein and not otherwise defined have the meanings ascribed to such terms in the Official Statement.

Based on the information set forth in this Official Statement, our experience and our analyses during the preparation of the 1983 feasibility study, the methodology described below and subject to the reliances and assumptions made throughout this letter, Metcalf & Eddy concludes that overall the water and sewer system (the “System”) serving the City continues to be operated in a professional and prudent manner. Further, Metcalf & Eddy is of the opinion that:

- The condition of the System continues to receive the highest rating of our three rating categories (adequate).
- The expense allocations for Fiscal Year 2005 are adequate for the continued reliable operation of the System.
- The Capital Improvement Program (the “CIP”) is responsive to the long-term operating requirements of the service area.
- Staffing levels of the System are adequate for proper operation and maintenance.

Metcalf & Eddy hereby consents to the inclusion of those opinions and conclusions attributed to it in the Official Statement.

**Purpose and Scope**

This letter has been prepared to document the results of analyses carried out during the period of August 1983 to the present by personnel of Metcalf & Eddy in connection with the issuance of the Water and Sewer System Second General Resolution Revenue Bonds, Fiscal 2006 Series AA by the New York City Municipal Water Finance Authority (the “Authority”). Certain studies and analyses were performed in anticipation of the creation of the Authority and were used in developing the information in the Official Statement under the captions: “CAPITAL IMPROVEMENT AND FINANCING PROGRAM—Capital Improvement Program,” “THE SYSTEM—The Water System” and “THE SYSTEM—The Sewer System.” The following sets forth a brief outline of the major tasks addressed:

- An overview of the System’s service area and major facilities, including a general assessment of the capacity and condition of existing water, wastewater and drainage facilities and a review of recently completed improvements.
- An analysis of the CIP for the period 2005-2015 and the funding needed to carry out the CIP and ongoing capital contracts commenced prior to the CIP.
- An analysis of the management of the System and its current and anticipated operating programs.

Since 1983 Metcalf & Eddy has provided engineering services related to the City’s Water and Wastewater Operations Evaluation Study. During this period Metcalf & Eddy has performed an evaluation of the condition of the System, independently reviewed the capital plans for water and wastewater programs, and jointly with the rate consultant reviewed the operating programs of the New York City Department of Environmental Protection (“DEP”). Ten topics were addressed in this effort as listed below.

- Present Condition of Physical Facilities
- Remaining Useful Life of Facilities
- Reliability of Utility Systems
- Operation and Maintenance Programs
- Current Utility Use
- Maximum Existing Capacity
- Needs for Routine Maintenance, Upgrading and Expansion
- Evaluation of the Impact of Legal Mandates
- Overview of Present Capital Improvement Program
- Safety Practices and Potential for Catastrophe

### **Methodology**

Interviews with staff members of the Authority and the City were conducted, current engineering and financial reports, System operating data and other documents were reviewed and major facilities were inspected. Audited financial statements of the City and data supplied by the Authority were also reviewed to identify historical costs and revenues. The evaluation of current needs and future conditions was made by analyzing historical data, assessing the effectiveness of current City maintenance programs, reviewing the plans of key outside agencies, and taking into account current trends and the anticipated impact of the CIP.

The physical condition of the facilities was rated by Metcalf & Eddy. A uniform rating system, standard among engineering firms providing similar services, was established consisting of three rating categories—adequate, marginal, and inadequate as described below:

- Adequate: Shows no signs of deterioration, meets design intent, and requires only routine maintenance to meet or exceed expected useful life.
- Marginal: Facility is functional but does not meet design intent, and requires non-routine maintenance or capital replacement to restore to adequate condition.
- Inadequate: Facility does not provide functional operation, and requires major reconstruction to restore to adequate condition.

### **The Consulting Engineer**

Metcalf & Eddy has served the City as consulting engineers for over 90 years in capacities dealing with water supply, water distribution, sewage collection, and wastewater treatment. Metcalf & Eddy is one of the largest consulting engineering firms and is recognized in the United States and internationally as a leader in services to the water and wastewater industry.

We have no responsibility to update this letter or the information provided in the Official Statement for the captioned sections described above for events and circumstances occurring after the date of this letter.

Very truly yours,



/s/ James Anderson  
JAMES ANDERSON  
*President*  
Metcalf & Eddy of New York, Inc.



**LETTER OF AMAWALK CONSULTING GROUP LLC,  
RATE CONSULTANTS**

**Amawalk Consulting Group LLC  
New York, NY**

October 18, 2005

Mr. Alan L. Anders  
Executive Director  
New York City Municipal Water Finance Authority

Subject: New York City Municipal Water Finance Authority  
Water and Sewer System Second General Resolution Revenue Bonds  
Fiscal 2006 Series AA

Dear Mr. Anders:

The purpose of this letter is to summarize the conclusions of the independent analysis of the financial forecast of the Authority (the “Forecasted Cash Flows”) for Fiscal Years 2005 through 2010 (the “Reporting Period”) prepared by the Amawalk Consulting Group LLC in connection with the issuance by the New York City Municipal Water Finance Authority (the “Authority”) of the Authority’s \$400,000,000 Water and Sewer System Second General Resolution Revenue Bonds, Fiscal 2006 Series AA (the “Series AA Bonds”). Proceeds from the Series AA Bonds are expected to be used: (i) to pay principal and interest on a portion of the Authority’s Outstanding Commercial Paper Notes, (ii) to fund a portion of the Authority’s capital program and (iii) to pay certain costs of issuance. In conducting the analysis, the Amawalk Consulting Group LLC has prepared the following tables which are included in this Official Statement under the headings “Capital Improvement and Financing Program” and “Financial Operations.”

- Sources and Uses of Capital Funds
- Future Debt Service Requirements
- Projected Revenues
- Projected System Expense
- Forecasted Cash Flows

The forecast includes provisions for the financing of improvements to the City of New York (the “City”) Water and Sewer System (the “System”) as reflected in the Capital Improvement Program (the “CIP”) for the Reporting Period. The Forecasted Cash Flows set forth the ability of the System to meet the operating costs, working capital needs and other financial requirements of the System, including the debt service requirements associated with the Outstanding Bonds issued under the Authority’s General Bond Resolution (the “First Resolution”) and obligations issued under the Authority’s Second General Resolution (the “Second Resolution”) and additional First Resolution Bonds and Second Resolution Bonds whose issuance by the Authority during the five years ending June 30, 2010 is anticipated.

Revenues pledged to secure the Authority’s First Resolution Bonds are to be derived from the following sources: (i) all Revenues, (ii) all moneys or securities in any of the Funds and Accounts, and (iii) all other monies and securities to be received, held or set aside by the Authority or by any Fiduciary pursuant to the First Resolution. The term “Revenues”, as defined by the First Resolution, includes, but is not limited to, all rents, fees, charges and other income and receipts derived by the New York City Water Board (the “Board”) from users of the System, and certain investment proceeds received by the Board.

Moneys pledged to secure bonds issued under the Second Resolution are to be derived from: (i) all available amounts on deposit in the Subordinated Indebtedness Fund established under the First

Resolution and (ii) all moneys or securities in any of the funds and accounts established under the Second Resolution, except the Arbitrage Rebate Fund and the Debt Service Reserve Fund.

The Forecasted Cash Flows summarize the anticipated financial operations of the Authority for the Reporting Period. The Authority's books, records, financial reports, and statistical data have been reviewed to the extent practicable, and other investigations and analyses were conducted as deemed necessary to assemble and analyze the forecast of revenues, revenue requirements, and debt service coverage for the Reporting Period. Various financial tests and analyses have been performed to support the findings and conclusions presented herein. The Authority's fiscal year ends on June 30, and all references in the Official Statement to a fiscal year ("Fiscal Year") relate to the 12 month period ending June 30 of the year shown.

Proposed improvements and additions to the System under the CIP for the Reporting Period were independently evaluated and confirmed by Metcalf & Eddy of New York, Inc. ("Metcalf & Eddy"). The forecasted cash flows rely upon the conclusions of Metcalf & Eddy regarding the capital and operating expenditures that are necessary during the Reporting Period to maintain the System in good working order.

Based on the studies performed, the Amawalk Consulting Group LLC offers the following opinions and conclusions:

1. Revenues (including projected revenue increases resulting from anticipated future rate increases to be implemented by the Board), as set forth in the Forecasted Cash Flows, are currently and will be sufficient to meet the following requirements during the Reporting Period:

a. One hundred and fifteen percent (115%) of the principal of and interest on all First Resolution Bonds issued under the First Resolution, as the same shall become due and payable, for which such Revenues are pledged;

b. One hundred percent (100%) of the principal of and interest on all Second Resolution bonds issued under the Second Resolution and other subordinate obligations payable from Revenues;

c. One hundred percent (100%) of all expenses of operation, maintenance and repair of the System;

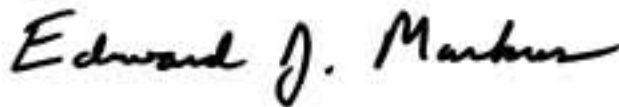
d. One hundred percent (100%) of other Required Deposits as required by the First Resolution. In addition, revenues are adequate to make all payments to the City.

2. In the analysis of the forecast of future operations summarized in this Official Statement, the Amawalk Consulting Group LLC has reviewed certain assumptions with respect to conditions, events and circumstances which may occur in the future. These assumptions are reasonable and attainable, although actual results may differ from those forecast as influenced by the conditions, events and circumstances which actually occur.

3. The water and wastewater rates, fees and charges of the Board, including projected increases, are reasonable and compare favorably to the rates and charges of other major cities.

The opportunity to be of service to the Authority in this important matter is greatly appreciated.

Very truly yours,



Edward J. Markus  
Amawalk Consulting Group LLC

## GLOSSARY AND SUMMARY OF CERTAIN DOCUMENTS

## GLOSSARY

Set forth below are definitions of certain terms contained in the Agreement, the Lease, the First Resolution and the Second Resolution, and not otherwise defined in this Official Statement. As used in this Official Statement, terms defined in both the First Resolution and the Second Resolution shall have the meanings specified in the First Resolution or the Second Resolution as the context requires.

**Definition of Certain Terms Used in First Resolution**

**Adjusted Aggregate Debt Service:** For any Fiscal Year and as of any date of calculation is the sum of the Adjusted Debt Service for all Series of Bonds Outstanding during such Fiscal Year.

**Adjusted Debt Service:** For any Fiscal Year, as of any date of calculation and with respect to any Series of Bonds, is the Debt Service for such Fiscal Year for such Series except that, if any Refundable Principal Installment of such Series of Bonds is included in Debt Service for such Fiscal Year, Adjusted Debt Service shall mean Debt Service determined as if each such Refundable Principal Installment had been payable over a period extending from the due date of such Refundable Principal Installment through the last date on which such Series of Bonds could have been stated to mature under the Act as in effect on the date of issuance of such Series, in installments which would have required equal annual payments of Principal Installments and interest over such period. Interest deemed payable in any Fiscal Year after the actual due date of any Refundable Principal Installment of any Series of Bonds shall be calculated at the actual interest cost payable on the Bonds of such Series (using the actuarial method of calculation).

**Aggregate Debt Service:** For any Fiscal Year, as of any date of calculation, the sum of the Debt Service for all Bonds Outstanding during such Fiscal Year.

**Authority Expenses:** All reasonable or necessary current expenses of the Authority, including all salaries, administrative, general, commercial, engineering, advertising, public notice, auditing and legal expenses, insurance and surety bond premiums, fees paid to banks, insurance companies or other financial institutions for the issuance of Credit Facilities, consultants' fees and charges, payment to pension, retirement, health and hospitalization funds, costs of public hearings, ordinary and current rentals of equipment and other property, lease payments for real property or interests therein, expenses, liabilities and compensation of any Fiduciary and all other expenses necessary, incidental or convenient for the efficient operation of the Authority. Bond Counsel has determined that payments made under an Interest Rate Exchange Agreement are deemed Authority Expenses if the Interest Rate Exchange Agreement relates to First Resolution Bonds.

**Authorized Newspaper:** The Bond Buyer or any other newspaper of general circulation printed in the English language and customarily published at least once a day for at least five days (other than legal holidays) in each calendar week in the Borough of Manhattan, City and State of New York, designated by the Authority.

**Authorized Representative:** In the case of both the Authority and the Board, their respective Chairman or Executive Director, or such other person or persons so designated by resolution of the Authority or the Board, as the case may be, and in the case of the City, the Mayor, unless a different City official is designated to perform the act or sign the document in question.

**Bond or Bonds:** For purposes of the Agreement and the Resolution (and as used in this Official Statement unless the context otherwise requires), the bonds, notes or other evidences of indebtedness issued by the Authority under and pursuant to the Act and the Resolution, including Parity Bond Anticipation Notes and Parity Reimbursement Obligations; but shall not mean Subordinated Indebtedness or other Bond Anticipation Notes or Reimbursement Obligations; and for purposes of the Lease, means any bonds, notes or other evidences of indebtedness for borrowed money issued by the Authority.

**Bond Counsel's Opinion:** An opinion signed by an attorney or firm of attorneys of nationally recognized standing in the field of law relating to revenue bonds of municipalities and public agencies, selected by the Authority and satisfactory to the Trustee.

**Bond Payment Date:** June 15 and December 15 of each year; provided, however, that if any such day is not a Business Day, then the Bond Payment Date shall be the next succeeding Business Day.

**Business Day:** Any day which is not a Saturday, Sunday or a day on which the New York Stock Exchange, banking institutions chartered by the State or the United States of America or the Note Trustee are legally authorized to close in the City.

**Cash Flow Requirement:** For each Fiscal Year and as of any date of certification, the amount, certified by the Authority to the Trustee and the Board equal to the difference between (A) the sum of (i) the estimated Aggregate Debt Service for such Fiscal Year, (ii) the Projected Debt Service for such Fiscal Year, (iii) the estimated Authority Expenses for such Fiscal Year, and (iv) the other Required Deposits estimated for such Fiscal Year and (B) (i) if the certification is made prior to the commencement of the Fiscal Year, the amount anticipated by the Authority as of such date of certification to be held by the Trustee, as of the first day of such Fiscal Year, in the Revenue Fund and (ii) if the certification is made after the commencement of such Fiscal Year, the amount which had been anticipated pursuant to (B) (i) above.

**Consulting Engineer:** Metcalf & Eddy of New York, Inc. or such other independent engineer or engineering firm of recognized standing selected by the Authority and satisfactory to the Board.

**Corporation:** The New York State Environmental Facilities Corporation and any successor entity which may succeed to its rights and duties respecting the State Revolving Fund.

**Cost or Costs of a Water Project:** The cost of construction, as such term is defined in the Act, including, without limiting the generality of the foregoing, the erection, alteration, improvement, increase, enlargement or rehabilitation of the System or a Water Project, the inspection and supervision thereof, the engineering, architectural, legal, fiscal, economic and environmental investigations and studies, designs, surveys, plans, specifications, procedures and other actions incidental thereto; the cost of the acquisition of all Property; the cost of demolishing, removing or relocating any buildings or structures on lands so acquired (including the cost of acquiring any lands to which such buildings or structures may be moved or relocated); the cost of all systems, facilities, machinery, appurtenances, equipment, financing charges and interest prior to, during and after construction (if not paid or provided for from revenues or other sources); the cost of engineering and architectural surveys, plans and specifications; the cost of consultants' and legal services; the cost of lease guarantee or bond insurance; other expenses necessary, reasonably related or incidental to the construction of such Water Project and the financing of the construction thereof, including the cost of Credit Facilities, the amounts authorized in the Resolution to be paid into any reserve or other special fund from the proceeds of Bonds and the financing or the placing of any Water Project in operation, including reimbursement to any governmental entity or any other person for expenditures that would be Costs of such Water Project and all claims arising from any of the foregoing.

**Counterparty:** An entity whose senior long term debt obligations, or whose obligations under an Interest Rate Exchange Agreement are guaranteed by a financial institution whose senior long term debt obligations, have a rating (at the time the subject Interest Rate Exchange Agreement is entered into) of Aa or better by Moody's Investors Service and AA or better by Standard & Poor's Ratings Services.

**Credit Facility:** A letter of credit, revolving credit agreement, standby purchase agreement, surety bond, insurance policy or similar obligation, arrangement or instrument issued by a bank, insurance company or other financial institution which provides for payment of all or a portion of the Principal Installments or interest due on any Series of Bonds or provides funds for the purchase of such Bonds or portions thereof.

**Debt Service:** For any Fiscal Year or part thereof, as of any date of calculation and with respect to any Series, means an amount equal to the sum of (a) interest payable during such Fiscal Year or part

thereof on Bonds of such Series, except to the extent that such interest is to be paid from amounts representing Capitalized Interest and (b) the Principal Installments of the Bonds of such Series payable during such Fiscal Year or part thereof. Such interest and Principal Installments for such Series shall be calculated on the assumption that (x) no Bonds of such Series Outstanding at the date of calculation will cease to be Outstanding except by reason of the payment thereof upon stated maturity or upon mandatory redemption by application of Sinking Fund Installments and (y) Variable Rate Bonds will bear interest at the greater of (A) the rate or rates which were assumed by the Authority in the Authority Budget for such Fiscal Year to be borne by Variable Rate Bonds during such Fiscal Year or (B) the actual rate or rates borne during such Fiscal Year on Variable Rate Bonds Outstanding during the 12 calendar months preceding the date of calculation.

**Debt Service Reserve Requirement:** As of any date of calculation, and for any Fiscal Year, shall mean the amount equal to the maximum Adjusted Aggregate Debt Service in the current or any future Fiscal Year on all Bonds Outstanding; provided, however, that, if (i) the payment of the Principal Installments of or interest on any Series of Bonds or portion thereof is secured by a Special Credit Facility, (ii) the payment of the Tender Option Price of any Option Bond of a Series is secured by a Special Credit Facility or (iii) the Authority has determined in a Supplemental Resolution authorizing the issuance of a Series of Bonds that such Series of Bonds will not be secured by the Common Account in the Debt Service Reserve Fund, the Supplemental Resolution authorizing such Series may specify the Debt Service Reserve Requirement, if any, for the Bonds of such Series.

**DEC:** The New York State Department of Environmental Conservation and any successor entity which may succeed to its rights and duties respecting the State Revolving Fund.

**Defeasance Obligations:** (A) any non-callable bonds or other obligations which as to principal and interest constitute direct obligations of, or are guaranteed by the United States of America, including obligations of any agency thereof or corporation which has been or may hereafter be created pursuant to an Act of Congress as an agency or instrumentality of the United States of America to the extent unconditionally guaranteed by the United States of America or (B) any other non-callable receipt, certificate or other evidence of an ownership interest in obligations or in specified portions thereof (which may consist of specified portions of the interest thereon) of the character described in subclause (A); provided, however, that, when used in connection with any Bond authorized to be issued by a Supplemental Resolution adopted on or after June 1, 2001, such term also means: (C) a non-callable obligation of the United States of America which has been stripped by the United States Department of Treasury itself or by any Federal Reserve Bank (not including "CATS," "TIGRS" and "TRS" unless the Authority obtains Rating Confirmation with respect to the Bonds to be defeased); (D) the interest component of REFCORP bonds for which separate payment of principal and interest is made by request of the Federal Reserve Bank of New York in book-entry form; (E) an obligation of any state or territory of the United States of America, any political subdivision of any state or territory of the United States of America, or any agency, authority, public benefit corporation or instrumentality of such state, territory or political subdivision (i) the interest on which is excludable from gross income under Section 103 of the Code, (ii) that, at the time an investment therein is made or such obligation is deposited in any fund or account established pursuant to the Resolution, is rated in the highest rating category of the Rating Agencies, (iii) that is not subject to redemption prior to maturity other than at the option of the holder thereof or either (1) has irrevocably been called for redemption or (2) as to which irrevocable instructions have been given to call such obligation on a stated future date and (iv) the timely payment of the principal or redemption price thereof and interest thereon is fully secured by a fund consisting only of cash or obligations described in clauses (A), (B), (C), (D), (E) or (F), which fund may be applied only to the payment of principal, interest and redemption premium, if any, on the obligation secured thereby; and (F) a non-callable note, bond, debenture, mortgage or other evidence of indebtedness that, at the time acquired, is (i) issued or guaranteed by the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, the Student Loan Marketing Association, the Federal Farm Credit System or any other instrumentality of the United States of America and (ii) rated in the highest rating category of the Rating Agencies; provided, further, that the term "Defeasance Obligations" shall not mean any interest in a unit investment trust or a mutual fund.

**Financial Guaranties:** One or more of the following: (i) irrevocable, unconditional and unexpired letters of credit issued by banking institutions the senior long-term debt obligations of which (or the holding company of any such banking institution) have (at the time of issue of such letter of credit) a rating of Aa2 or better by Moody's Investors Service and AA or better by Standard & Poor's Ratings Services; or (ii) an irrevocable and unconditional policy or policies of insurance in full force and effect issued by municipal bond insurers the obligations insured by which are eligible for a rating of Aa or better by Moody's Investors Service and AA or better by Standard & Poor's Ratings Services; in each case providing for the payment of sums for the payment of Principal Installments of an interest on Bonds in the manner provided in the Resolution; and providing further that any Financial Guaranty of the type described in (i) above must be drawn upon, on a date which is at least thirty (30) days prior to the expiration date of such Financial Guaranty, in an amount equal to the deficiency which would exist if the Financial Guaranty expired, unless a substitute Financial Guaranty is acquired prior to such expiration date as provided in a related Supplemental Resolution.

**Fiscal Year:** The twelve-month period commencing on July 1 of each year; provided, however, that the Authority, the Board and the City may agree on a different twelve-month period as the Fiscal Year and in such event the dates set forth in the Agreement, the Lease and the Resolution shall be adjusted accordingly.

**Government Obligation:** A direct obligation of the United States of America, an obligation the principal of, and interest on which are guaranteed as to full and timely payment by the United States of America, an obligation (other than an obligation subject to variation in principal repayment) to which the full faith and credit of the United States of America are pledged, an obligation of a federal agency guaranteed as to full and timely payment by the United States of America and approved by the Authority, and a certificate or other instrument which evidences the ownership of, or the right to receive all or a portion of the payment of, the principal of or interest on, direct obligations of the United States of America.

**Interest Rate Exchange Agreement:** Any financial arrangement (i) that is entered into by the Authority with an entity that is a Counterparty at the time the arrangement is entered into; (ii) which provides that the Authority shall pay to such entity an amount based on the principal amount of a Series of Bonds, and that such entity shall pay to the Authority an amount based on the principal amount of such Series of Bonds, in each case computed in accordance with a formula set forth in such agreement, or that one shall pay to the other any net amount due under such arrangement; (iii) which has been designated in writing to the Trustee by an Authorized Representative of the Authority as an Interest Rate Exchange Agreement with respect to a Series of Bonds and (iv) which, in the opinion of Bond Counsel, will not adversely affect the exclusion of interest on Bonds from gross income for the purposes of federal income taxation.

**Investment Securities** shall mean and include any of the following securities, if and to the extent the same are at the time legal investments by the Authority of the funds to be invested therein and conform to the policies set forth in any investment guidelines adopted by the Authority and in effect at the time of the making of such investment:

(i) direct obligations of, or obligations guaranteed as to principal and interest by, the State or direct obligations of any agency or public authority thereof, provided such obligations are rated, at the time of purchase, in one of the two highest rating categories by each Rating Agency then maintaining a rating on Outstanding Bonds;

(ii) (A) any bonds or other obligations which as to principal and interest constitute direct obligations of, or are guaranteed by the United States of America, including obligations of any agency thereof or corporation which has been or may hereafter be created pursuant to an Act of Congress as an agency or instrumentality of the United States of America to the extent unconditionally guaranteed by the United States of America or (B) any other receipt, certificate or other evidence of an ownership interest in obligations or in specified portions thereof (which may consist of specified portions of the interest thereon) of the character described in subclause (A) of this clause (ii);

(iii) obligations of any agency, subdivision, department, division or instrumentality of the United States of America; or obligations fully guaranteed as to interest and principal by any agency, subdivision, department, division or instrumentality of the United States of America;

(iv) banker's acceptances or certificates of deposit issued by a commercial bank (A) whose long-term debt obligations are rated by each Rating Agency then maintaining a rating on the Outstanding Bonds at least equal to the rating on Outstanding Bonds that are not insured or otherwise secured by a Credit Facility or a Special Credit Facility, (B) that has its principal place of business within the State and (C) that has capital and surplus of more than \$100,000,000;

(v) corporate securities, including commercial paper and fixed income obligations, which are, at the time of purchase, rated by each Rating Agency then maintaining a rating on Outstanding Bonds in its highest rating category for comparable types of obligations;

(vi) repurchase agreements collateralized by securities described in clauses (ii) or (iii) above with any registered broker/dealer or with any domestic commercial bank whose long-term debt obligations are rated "investment grade" by each Rating Agency then maintaining a rating on Outstanding Bonds, provided that (1) a specific written repurchase agreement governs the transaction, (2) the securities are held, free and clear of any lien, by the Trustee or an independent third party acting solely as agent for the Trustee, and such third party is (a) a Federal Reserve Bank, or (b) a bank which is a member of the Federal Deposit Insurance Corporation and which has combined capital, surplus and undivided profits of not less than \$25 million, and the Trustee shall have received written confirmation from such third party that it holds such securities, free and clear of any lien, as agent for the Trustee, (3) the repurchase agreement has a term of thirty days or less, or the Trustee will value the collateral securities no less frequently than monthly and will liquidate the collateral securities if any deficiency in the required collateral percentage is not restored within five business days of such valuation, (4) the fair market value of the collateral securities in relation to the amount of the repurchase obligation, including principal and interest, is equal to at least 102% and (5) the repurchase agreement meets the guidelines then applicable to such investments of each Rating Agency then maintaining a rating on Outstanding Bonds;

(vii) investment agreements or guaranteed investment contracts with any financial institution whose senior long term debt obligations, or whose obligations under such an investment agreement or guaranteed investment contract, are guaranteed by a financial institution whose senior long term debt obligations, have a rating (at the time such agreement or contract is entered into) in one of the two highest rating categories for comparable types of obligations by each Rating Agency then maintaining a rating on the Bonds;

(viii) money market funds rated in the highest rating category for comparable types of obligations by each Rating Agency then maintaining a rating on the Bonds; and

(ix) municipal obligations, the payment of principal and redemption price, if any, and interest on which is irrevocably secured by obligations of the type referred to in clauses (i), (ii) or (iii) above and which obligations have been deposited in an escrow arrangement which is irrevocably pledged to the payment of such municipal obligations and which municipal obligations are rated in the highest rating category for comparable types of obligations by each Rating Agency then maintaining a rating on the Bonds.

**Leased Property:** The real and personal property and other rights therein leased by the City to the Board pursuant to Article II of the Lease.

**Local Water Fund:** The special trust fund by that name established by the Act in the custody of the Board into which all Revenues are required to be deposited promptly upon receipt thereof by the Board.

**Minimum Monthly Balance:** For each Series of Bonds Outstanding, the monthly amount calculated in accordance with Section 4.3(a) of the Agreement. See "Summary of Certain Documents—Summary of the Agreement—Minimum Monthly Balance" in this Appendix C.

**O&M Reserve Fund Requirement:** For each Fiscal Year, the amount equal to one-sixth (1/6) of the Operating Expenses as set forth in the Annual Budget.

**Operating Expenses:** All reasonable or necessary current expenses of maintaining, repairing, operating and managing the System net of governmental operating aid, including: all salaries; administrative, general, commercial, architectural, engineering, advertising, public notice, auditing, billing, collection, enforcement and legal expenses; insurance and surety bond premiums; consultants' fees; payments to pension, retirement, health and hospitalization funds; taxes; payments in lieu of taxes; costs of public hearings; ordinary and current rentals of equipment or other property; hydrant rentals; lease payments for real property or interests therein (excluding certain amounts paid by the Board to the City pursuant to the Lease); depository expenses; reasonable reserves for maintenance and repair and all other expenses necessary, incidental or convenient for the efficient operation of the System; but only to the extent properly attributable to the Board or the System and payable by the Board to the City pursuant to the Lease and, except for certain administrative expenses of the Board, payable by the Board to the City pursuant to the Lease.

**Option Bonds:** Bonds which by their terms may be tendered by and at the option of the owner thereof for payment by the Authority prior to the stated maturity thereof, or the maturates of which may be extended by and at the option of the owner thereof.

**Outstanding:** As of any date, all Bonds therefore or thereupon being authenticated and delivered under the Resolution except:

- (a) any Bonds canceled by the Trustee at or prior to such date;
- (b) any Bond (or portion thereof) for the payment or redemption of which there shall be set aside and held in trust under the Resolution either:
  - (i) moneys in an amount sufficient to pay when due the Principal Installments or Redemption Price thereof, together with all accrued interest,
  - (ii) Defeasance Obligations in such principal amounts, of such maturities, bearing such interest and otherwise having such terms and qualifications, as are necessary to provide moneys (whether as principal or interest) in an amount sufficient to pay when due the Principal Installments or Redemption Price thereof, together with all accrued interest, or
  - (iii) any combination of (i) and (ii) above,

and, if such Bond or portion thereof is to be redeemed, for which notice of redemption has been given as provided in Article VI of the Resolution or provision satisfactory to the Trustee has been made for the giving of such notice;

- (c) any Bond in lieu of or in substitution for which other Bonds have been authenticated and delivered; and
- (d) any Bond deemed to have been paid as provided in Section 1201(b) of the Resolution.

**Parity Bond Anticipation Notes:** Bond Anticipation Notes the interest on which is payable from and secured by a pledge of, and a lien on, a parity with all other Bonds.

**Permitted Encumbrances:** When used with reference to the System, (i) any and all liens, encumbrances, security interests or other defects in or clouds on title existing on the Effective Date, (ii) the Lease, (iii) easements, rights of way and exceptions which do not materially impair the operation or maintenance of the Leased Property or the Revenues therefrom, (iv) mechanics', materialmen's, warehousemen's and other similar liens, as permitted by law and liens for taxes at the time not delinquent or being contested and (v) agreements for the sale and leaseback of elements of the System.

**Principal Installment:** As of any date of calculation and with respect to any Series, so long as any Bonds thereof are Outstanding, (i) the principal amount of Bonds (including (x) any amount designated in, or determined pursuant to, the applicable Supplemental Resolution, as the "principal amount" with respect to any Bonds which do not pay full current interest for all or any part of their term) (y) the Tender



Option Price of any Option Bonds which may be tendered for purchase or payment prior to the stated maturity thereof in accordance with the terms of the Supplemental Resolution authorizing such Option Bonds, unless such amount is secured by a Credit Facility which is not in default and (z) the principal amount of any Parity Reimbursement Obligations of such Series due (or so tendered for payment) on a certain future date for which no Sinking Fund Installments have been established, or (ii) the unsatisfied balance of any Sinking Fund Installments due on a certain future date for Bonds of such Series, or (iii) if such future dates coincide as to different Bonds of such Series, the sum of such principal amount of Bonds and of such unsatisfied balance of Sinking Fund Installments due on such future date. "Principal Installment" does not include the principal of Parity Bond Anticipation Notes.

**Project Financing Agreement:** Any Project Financing Agreement to be entered into among the Authority, the City, DEC and the Corporation pursuant to the State Revolving Fund Act.

**Projected Debt Service:** For any Fiscal Year or part thereof means, as of any date of calculation and with respect to any Projected Series of Bonds, an amount, certified by the Authority to the Trustee and the Board, as provided in the Agreement, equal to the Debt Service estimated by the Authority to be payable during such Fiscal Year on such Projected Series.

**Projected Series of Bonds:** Any Series of Bonds described in an Authority Budget as anticipated to be issued in the Fiscal Year to which such Authority Budget relates.

**Rate Consultant:** The independent accountant or firm of independent accountants, or a management consultant or firm of management consultants, or independent engineer or firm of independent engineers, having, in any case, a recognized standing in the field of water and sewer system consulting selected by the Authority and satisfactory to the Board. The Rate Consultant may be the same firm as the Consulting Engineer.

**Rating Agencies:** Moody's Investors Service and Standard & Poor's Ratings Services and their respective successors and assigns.

**Rating Confirmation:** A written confirmation of each Rating Agency to the effect that the rating assigned to each of the Bonds rated by such Rating Agency will remain unchanged and will not be withdrawn, suspended or reduced as a consequence of some act or occurrence.

**Redemption Price:** When used with respect to a Bond or portion thereof, the principal amount thereof plus the applicable premium, if any, payable upon either optional or mandatory redemption thereof pursuant to the Resolution.

**Refundable Principal Installment:** Any Principal Installment for any Series of Bonds which the Authority intends to pay with moneys which are not Revenues, provided that such intent shall have been expressed in the Supplemental Resolution authorizing such Series of Bonds and provided further that such Principal Installment shall be a Refundable Principal Installment only through the date of the Authority Budget adopted during the Fiscal Year immediately preceding the Fiscal Year in which such Principal Installment comes due unless the Authority has delivered to the Trustee a certificate of an Authorized Representative that it has made provision for the payment of such Principal Installment from a source other than Revenues.

**Refunding Bond:** Any Bond authenticated and delivered on original issuance pursuant to Section 206 or Section 207 of the Resolution for the purpose of refunding any Outstanding Bonds or thereafter authenticated and delivered in lieu of or substitution for such Bond pursuant to the Resolution.

**Reimbursement Obligation:** The obligation of the Authority described in the Resolution to directly reimburse the issuer of a Credit Facility for amounts paid by such issuer thereunder, whether or not such obligation to so reimburse is evidenced by a promissory note or other similar instrument.

**Required Deposits:** For any Fiscal Year, amounts, if any, payable into the Authority Expense Fund, the Debt Service Reserve Fund and the Subordinated Indebtedness Fund but only to the extent such payments are required to be made from Revenues pursuant to the Resolution.

**Revenues** shall mean (a) all the rents, fees, charges, payments and other income and receipts derived by the Board from users of the System, together with all operating aid therefor from any governmental entity, federal, State or local, to the Board, (b) investment proceeds and proceeds of insurance received by the Board (other than the proceeds of insurance with respect to the damage or destruction of all or any portion of the System), (c) Subsidy Payments derived by the Authority, (d) amounts derived by the Authority from a Counterparty pursuant to an Interest Rate Exchange Agreement, and (e) investment proceeds derived from amounts on deposit in the Funds and Accounts established hereunder that are deposited or retained in the Revenue Fund or the Local Water Fund, and but shall not include (w) amounts required to be refunded because of billing or payment errors, (x) any amount attributable to any of the foregoing sources described in clause (a) which (i) is expressly excluded by the Agreement or the Lease, or (ii) is derived from a use of the System not directly related to the supply, treatment and distribution of water to the consumers thereof or the collection, disposal or treatment of sewage, (y) any amount from any governmental entity, federal, State or local, in aid of or for or with respect to the Costs of Water Projects, other than Subsidy Payments, or (z)(i) fines (excluding interest on late payments which shall constitute Revenues), (ii) amounts from the use of water to generate electricity, (iii) amounts from the State as a result of mandatory water discharges from reservoirs or (iv) amounts from the granting of easements, licenses, rights-of-way or other interests in the real property constituting a part of the System.

**Special Credit Facility:** With respect to any Series of Bonds or portion thereof, a Credit Facility (a) which provides funds for (i) the direct payment of the Principal Installments of and interest on such Bonds when due or (ii) the payment of the Principal Installments of and interest on such Bonds in the event amounts otherwise pledged to the payment thereof are not available when due or (iii) the payment of the Tender Option Price of any Option Bond which may be tendered to the Authority for purchase or payment in accordance with the Supplemental Resolution authorizing such Option Bond (in any case, regardless of whether such Credit Facility provides funds for any other purpose) and (b) which (i) requires the Authority to directly reimburse the issuer of such Credit Facility for amounts paid thereunder and (ii) provides that such obligation is a Parity Reimbursement Obligation.

**State:** The State of New York.

**State Revolving Fund:** The New York State Water Pollution Control Revolving Fund established pursuant to the State Revolving Fund Act.

**State Revolving Fund Act:** Chapter 565 of the laws of New York of 1989, as amended.

**Subordinated Indebtedness:** Any bond, note or other evidence issued by the Authority in furtherance of its corporate purposes under the Act and payable from the subordinated Indebtedness Fund.

**Subsidy Payments** shall mean amounts payable to the Authority from any governmental entity, federal, State or local, in connection with Bonds of the Authority.

**Supplemental Resolution:** A resolution of the Authority authorizing the issuance of a Series of Bonds or otherwise amending or supplementing the Resolution.

**System:** The Water System and the Sewerage System, collectively, as such terms are defined in the Act.

**Tender Option Price:** With respect to any Option Bond tendered for purchase or payment, an amount equal to the principal amount thereof plus interest accrued and unpaid thereon from the immediately preceding Bond Payment Date to the date of such tender.

**Trustee:** The trustee appointed by the Authority pursuant to the Resolution, and any successors thereto.

**Variable Rate Bond:** As of any date of determination, any Bond on which the interest rate borne thereby may vary during any part of its remaining term.

**Water Project:** Any sewerage facility, water facility or water and sewerage facility, as the case may be, including the planning, development, financing or construction thereof.

## **Definition of Certain Terms Used in Second Resolution**

The following are definitions of certain terms contained in the Second Resolution:

**“Account”** shall mean one of the special accounts created and established pursuant to Article V of the Second Resolution.

**“Adjusted Aggregate Debt Service”** for any Fiscal Year, as of any date of calculation, unless used in relation to First General Resolution Bonds, shall mean the sum of the Adjusted Debt Service payable during such Fiscal Year for all Outstanding Bonds of a Series, Parity Bond Anticipation Notes and Parity Reimbursement Obligations, and, when used in relation to First General Resolution Bonds, shall have the meaning ascribed thereto in the First General Resolution.

**“Adjusted Debt Service”** for any Fiscal Year, as of any date of calculation, unless used in relation to First General Resolution Bonds, shall mean the sum of (a) the Debt Service for such Fiscal Year with respect to the Bonds of a Series except that, if any Refundable Principal Installment of such Series of Bonds is included in Debt Service for such Fiscal Year, Adjusted Debt Service shall mean Debt Service determined as if such Refundable Principal Installment had been payable over a period extending from the due date of such Refundable Principal Installment through the last date on which such Series of Bonds could have been stated to mature under the Act as in effect on the date of issuance of such Series, in installments which would have required equal annual payments of Principal Installments and interest over such period, (b) the Debt Service for such Fiscal Year with respect to Outstanding Parity Bond Anticipation Notes and (c) the Debt Service for such Fiscal Year with respect to Parity Reimbursement Obligations; and, when used in relation to First General Resolution Bonds, shall have the meaning ascribed thereto in the First General Resolution. Interest deemed payable in any Fiscal Year after the actual due date of any Refundable Principal Installment of any Series of Bonds shall be calculated at the actual interest cost on all Bonds of such Series (using the actuarial method of calculation).

**“Aggregate Debt Service”** for any Fiscal Year, as of any date of calculation, unless used in relation to First General Resolution Bonds, shall mean the sum of (a) the Debt Service for all Bonds Outstanding during such Fiscal Year, (b) the interest payable during such Fiscal Year on all Parity Bond Anticipation Notes Outstanding during such Fiscal Year and (c) the Debt Service payable during such Fiscal Year on all Parity Reimbursement Obligations Outstanding during such Fiscal Year; and, when used in relation to First General Resolution Bonds, shall have the meaning ascribed thereto in the First General Resolution.

**“Arbitrage Rebate Fund”** shall mean the fund by that name established pursuant to the Resolution.

**“Authority Budget”** shall mean the annual budget of the Authority, as amended or supplemented, adopted or in effect for a particular Fiscal Year, as provided in the Resolution.

**“Authority Expense Fund”** shall mean the fund by that name established pursuant to the Resolution.

**“Authorized Representative”** shall mean (i) in the case of both the Authority and the Board, their respective Chairman or Executive Director, or such other person or persons so designated by resolution of the Authority or the Board, as the case may be, and (i) in the case of the City, the Mayor, unless a different City official is designated in the Resolution or in a Supplemental Resolution to perform the act or sign the document in question.

**“Board”** shall mean the New York City Water Board, a body corporate and politic constituting a corporate municipal instrumentality of the State created and existing under and by virtue of the Act.

**“Bond”** or **“Bonds”** shall mean any of the bonds authenticated and delivered pursuant to the Resolution.

**“Bond Anticipation Note”** shall mean any note authorized to be issued under a resolution adopted pursuant to the Resolution.

**“Bond Counsel’s Opinion”** or **“Opinion of Bond Counsel”** shall mean an opinion signed by Orrick, Herrington & Sutcliffe LLP or by any other attorney or firm of attorneys of nationally recognized standing in the field of law relating to revenue bonds of municipalities and public agencies, selected by the Authority and satisfactory to the Trustee.

**“Bond Payment Date”** shall mean each date on which interest or both a Principal Installment and interest shall be due and payable on any of the Outstanding Bonds, Parity Bond Anticipation Notes or Parity Reimbursement Obligations according to their respective terms.

**“Bondholder”, “Owner” or “Holder”** or words of similar import shall mean, when used with reference to a Bond, the person in whose name the Bond is registered.

**“Capitalized Interest”** shall mean (i) for any particular Series, that portion of the proceeds of the Bonds of such Series, if any, required by the Supplemental Resolution authorizing such Series to be deposited in a sub-account established for such Series in the Capitalized Interest Account of the Debt Service Fund, for the purpose of funding the payment of a portion of the interest on the Bonds of such Series and (ii) for any Parity Bond Anticipation Notes, that portion of the proceeds of such Parity Bond Anticipation Notes, if any, required by the resolution authorizing such Bond Anticipation Notes to be deposited in a sub-account established for such Parity Bond Anticipation Notes in the Capitalized Interest Account of the Debt Service Fund, for the purpose of funding the payment of interest on such Bond Anticipation Notes.

**“Capitalized Interest Account”** shall mean the account by that name established in the Debt Service Fund pursuant to the Resolution.

**“Cash Flow Requirement”** shall mean, for each Fiscal Year and as of any date of certification, the amount, certified by the Authority to the Trustee and the Board as provided in the Agreement, equal to the difference between (a) the sum of (i) the estimated Aggregate Debt Service for such Fiscal Year on First General Resolution Bonds, (ii) the Projected Debt Service for such Fiscal Year on First General Resolution Bonds, (iii) the SGR Cash Flow Requirement for such Fiscal Year, (iv) the estimated Authority Expenses for such Fiscal Year and (v) the other Required Deposits estimated for such Fiscal Year and (b) (i) if such certification is made prior to the commencement of such Fiscal Year, the amount anticipated by the Authority as of such date of certification to be held as of the first day of such Fiscal Year, in the FGR Revenue Fund and (ii) if such certification is made after the commencement of such Fiscal Year, the amount described in subclause (i) of this clause (b).

**“City”** shall mean The City of New York.

**“Code”** shall mean the Internal Revenue Code of 1986, as amended, or any successor thereto, as the same may be in effect from time to time.

**“Common Account”** shall mean the account by that name established in the Debt Service Reserve Fund pursuant to the Resolution.

**“Construction Account”** shall mean the account by that name established in the FGR Subordinated Indebtedness Fund pursuant to the Resolution.

**“Construction Fund”** shall mean the fund by that name established pursuant to the Resolution.

**“Consulting Engineer”** shall mean Metcalf & Eddy of New York, Inc. or such other independent engineer or firm of engineers of recognized standing selected by the Authority and satisfactory to the Board and may include an independent engineer or firm of engineers retained by the City in one or more other capacities.

**“Costs” or “Costs of a Water Project”** shall mean the cost of “construction”, as such term is defined in the Act including, without limiting the generality of the foregoing, the erection, building, alteration, improvement, increase, enlargement, extension, reconstruction, renovation or rehabilitation of the System or a Water Project, the inspection and supervision thereof, the engineering, architectural, legal, fiscal, economic and environmental investigations and studies, surveys, designs, plans, working drawings, specifications, procedures and other actions incidental thereto; the cost of the acquisition of all property; the cost of demolishing, removing or relocating any buildings or structures on lands so acquired, including the cost of acquiring any lands to which such buildings or structures may be moved or relocated; the cost of all systems, facilities, machinery, apparatus and equipment, financing charges, interest prior to, during and after construction to the extent not paid or provided for from revenues or other sources; the cost of

engineering and architectural surveys, plans and specifications; the cost of consultants' and legal services; the cost of lease guarantee or bond insurance, other expenses necessary, reasonably related or incidental to the construction of such Water Project and the financing of the construction thereof, including the cost of Credit Facilities, the amounts authorized in the Resolution to be paid into any reserve or other special fund from the proceeds of Bonds and the financing of the placing of any Water Project in operation, including reimbursement to any municipality, any state agency, the State, the United States of America, or any other person for expenditures that would be costs of such Water Project under the Resolution and all claims arising from any of the foregoing.

**“Costs of Issuance”** shall mean all items of expense directly or indirectly payable or reimbursable and related to the authorization, sale and issuance of Bonds, including but not limited to printing costs, costs of preparation and reproduction of documents, filing and recording fees, initial fees and charges of any Fiduciary, legal fees and charges, fees and disbursements of consultants and professionals, costs of credit ratings, fees and charges for preparation, execution, transportation and safekeeping of Bonds, costs and expenses of refunding, premiums for the insurance of the payment of the Bonds and any other cost, charge or fee in connection with the original issuance of Bonds.

**“Counterparty”** shall mean an entity (i) whose senior long term debt obligations are rated (at the time the subject Interest Rate Exchange Agreement is entered into) in either of the two highest rating categories from a recognized statistical rating organization or (ii) whose obligations under an Interest Rate Exchange Agreement are guaranteed by a financial institution whose senior long term debt obligations are rated (at the time the subject Interest Rate Exchange Agreement is entered into) in either of the two highest rating categories from a nationally recognized statistical rating organization or (iii) whose obligation, if any, to make payment to the Authority upon termination of the Interest Rate Exchange Agreement is fully collateralized by Investment Securities of the type described in clause (ii) of the definition of Investment Securities, provided however, that such obligation shall be deemed to be fully collateralized if the Investment Securities shall have a market value, determined periodically in accordance with the Interest Rate Exchange Agreement, that is not less than the termination payment by any amount not greater than .1% of the Revenues for the preceding Fiscal Year.

**“Credit Facility”** shall mean a letter of credit, revolving credit agreement, standby purchase agreement, surety bond, insurance policy or similar obligations, arrangement or instrument issued by a bank, insurance company or other financial institution which (i) provides for payment of all or a portion of the Principal Installments or interest due on any Series of Bonds or on Parity Bond Anticipation Notes, (ii) provides funds for the purchase of such Bonds or portions thereof or (iii) secures the payment by the Authority of its obligations under an Interest Rate Exchange Agreement relating to Bonds.

**“Debt Service”** for any Fiscal Year or part thereof shall mean, as of any date of calculation (i) with respect to the Outstanding Bonds of any Series, an amount equal to the sum of (a) interest payable during such Fiscal Year or part thereof on such Bonds, except to the extent that such interest is to be paid from amounts representing Capitalized Interest and (b) the Principal Installments of such Bonds payable during such Fiscal Year or part thereof; (ii) with respect to Outstanding Parity Bond Anticipation Notes, interest payable thereon during such Fiscal Year or part thereof, except to the extent that such interest is to be paid from amounts representing Capitalized Interest; and (iii) with respect to a Parity Reimbursement Obligation, an amount equal to the sum of (a) interest payable during such Fiscal Year or part thereof on such Parity Reimbursement Obligation and (b) the Principal Installments of such Parity Reimbursement Obligation payable during such Fiscal Year or part thereof. Such interest and Principal Installment shall be calculated on the assumption that (x) no such Bonds, Parity Bond Anticipation Notes or Parity Reimbursement Obligations Outstanding at the date of calculation will cease to be Outstanding except by reason of the payment thereof upon stated maturity or upon mandatory redemption by application of Sinking Fund Installments and (y) Variable Rate Bonds will bear interest at the greatest of (A) the rate or rates which were assumed by the Authority in the Authority Budget for such Fiscal Year to be borne by Variable Rate Bonds during such Fiscal Year or (B) the average rate or rates borne during such Fiscal Year on Variable Rate Bonds Outstanding during the twelve calendar months preceding the date of calculation; provided, however, that if the Authority has in connection with any Variable Rate Bonds entered into an Interest Rate Exchange Agreement which provides that the Authority is to pay to

the Counterparty an amount determined based upon a fixed rate of interest on the Outstanding principal amount of such Variable Rate Bonds or that the Counterparty is to pay to the Authority an amount determined based upon the amount by which the rate at which such Variable Rate Bonds bear interest exceeds a stated rate of interest on all or any portion of such Variable Rate Bonds, it will be assumed that such Variable Rate Bond bears interest at the fixed rate of interest to be paid by the Authority or the rate in excess of which the Counterparty is to make payment to the Authority in accordance with such agreement.

**“Debt Service Fund”** shall mean the fund by that name established pursuant to the Resolution.

**“Debt Service Reserve Fund”** shall mean the fund by that name established pursuant to the Resolution.

**“Debt Service Reserve Requirement”** shall mean, as of any date of calculation, and for any Fiscal Year, the amount equal to the maximum Adjusted Aggregate Debt Service on Bonds in the current or any future Fiscal Year on all Bonds Outstanding; *provided, however*, that if, upon the issuance of a Series of Bonds, such amount would require moneys, in an amount in excess of the maximum amount permitted under the Code to be deposited therein from the proceeds of such Bonds, to be deposited therein, the Debt Service Reserve Requirement shall mean an amount equal to the sum of the Debt Service Reserve Requirement immediately preceding issuance of such Bonds and the maximum amount permitted under the Code to be deposited therein from the proceeds of such Bonds, as certified by an Authorized Representative of the Authority; *provided, further*, that, if (i) the payment of the Principal Installments of or interest on any Series of Bonds or portion thereof is secured by a Special Credit Facility, (ii) the payment of the Tender Option Price of any Option Bond of a Series is secured by a Special Credit Facility or (iii) the Authority has determined in a Supplemental Resolution authorizing the issuance of a Series of Bonds that such Series of Bonds will not be secured by the Common Account in the Debt Service Reserve Fund, the Supplemental Resolution authorizing such Series may specify the Debt Service Reserve Requirement, if any, for the Bonds of such Series; *provided, further*, that if, as a result of the expiration or termination of a Financial Guaranty, a deficiency shall be created in the Debt Service Reserve Fund, the Debt Service Reserve Requirement shall be calculated so as to exclude the amount of such deficiency and the Debt Service Reserve Requirement shall be increased in each of the five Fiscal Years after the date such deficiency was created by an amount equal twenty per centum (20%) of the aforesaid deficiency.

For the purpose of calculating the Debt Service Reserve Requirement for any Variable Rate Bonds of a Series, the maximum Adjusted Debt Service on such Series shall be determined by reference to the Pro Forma Bond Issue for the Variable Rate Bonds of such Series set forth in the Supplemental Resolution authorizing such Series.

**“Defeasance Obligations”** (A) any non-callable bonds or other obligations which as to principal and interest constitute direct obligations of, or are guaranteed by the United States of America, including obligations of any agency thereof or corporation which has been or may hereafter be created pursuant to an Act of Congress as an agency or instrumentality of the United States of America to the extent unconditionally guaranteed by the United States of America or (B) any other non-callable receipt, certificate or other evidence of an ownership interest in obligations or in specified portions thereof (which may consist of specified portions of the interest thereon) of the character described in subclause (A); (C) a non-callable obligation of the United States of America which has been stripped by the United States Department of Treasury itself or by any Federal Reserve Bank (not including “CATS,” “TIGRS” and “TRS” unless the Authority obtains Rating Confirmation with respect to the Bonds to be defeased); (D) the interest component of REFCORP bonds for which separate payment of principal and interest is made by request of the Federal Reserve Bank of New York in book-entry form; (E) an obligation of any state or territory of the United States of America, any political subdivision of any state or territory of the United States of America, or any agency, authority, public benefit corporation or instrumentality of such state, territory or political subdivision (i) the interest on which is excludable from gross income under Section 103 of the Code, (ii) that, at the time an investment therein is made or such obligation is deposited in any fund or account established pursuant to the Resolution, is rated in the highest rating category of

the Rating Agencies, (iii) that is not subject to redemption prior to maturity other than at the option of the holder thereof or either (1) has irrevocably been called for redemption or (2) as to which irrevocable instructions have been given to call such obligation on a stated future date and (iv) the timely payment of the principal or redemption price thereof and interest thereon is fully secured by a fund consisting only of cash or obligations described in clauses (A), (B), (C), (D), (E) or (F), which fund may be applied only to the payment of principal, interest and redemption premium, if any, on the obligation secured thereby; and (F) a non-callable note, bond, debenture, mortgage or other evidence of indebtedness that, at the time acquired, is (i) issued or guaranteed by the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, the Student Loan Marketing Association, the Federal Farm Credit System or any other instrumentality of the United States of America and (ii) rated in the highest rating category of the Rating Agencies; provided, further, that the term “Defeasance Obligations” shall not mean any interest in a unit investment trust or a mutual fund.

“**Depository**” shall mean any bank or trust company selected by the Board or the Authority, as the case may be, as a depository of moneys to be held under the provisions of the Agreement or the Resolution, and may include the Trustee.

“**Event of Default**” shall mean any event specified as an event of default in the Resolution.

“**FGR Authority Expense Fund**” shall mean the Authority Expense Fund established pursuant to the First General Resolution.

“**FGR Construction Fund**” shall mean the Construction Fund established pursuant to the First General Resolution.

“**FGR Debt Service Reserve Fund**” shall mean the Debt Service Reserve Fund established pursuant to the First General Resolution.

“**FGR Debt Service Fund**” shall mean the Debt Service Fund established pursuant to the First General Resolution.

“**FGR Revenue Fund**” shall mean the Revenue Fund established pursuant to the First General Resolution.

“**FGR Subordinated Indebtedness Fund**” shall mean the Subordinated Indebtedness Fund established pursuant to the First General Resolution.

“**Fiduciary**” shall mean the Trustee or any Paying Agent or Depository.

“**Financial Guaranty**” shall mean a surety bond, insurance policy or letter of credit which constitutes any part of the Debt Service Reserve Requirement and which is authorized to be delivered to the Trustee pursuant to the Resolution.

“**Financial Guaranty Provider**” shall mean the issuer of any Financial Guaranty.

“**First General Resolution**” shall mean the Water and Sewer System General Revenue Bond Resolution adopted by the Authority on November 14, 1985 as amended and supplemented in accordance therewith and as the same may be amended or supplemented in accordance therewith and the Resolution.

“**First General Resolution Bond**” shall mean a bond, note or other evidence of indebtedness issued pursuant to the First General Resolution, including a “Parity Bond Anticipation Note” and a “Parity Reimbursement Obligation,” as such terms are defined in the First General Resolution.

“**Fiscal Year**” shall have the meaning ascribed to such term in the Agreement.

“**Fund**” shall mean any fund established pursuant to Resolution.

“**Interest Rate Exchange Agreement**” means an agreement entered into by the Authority relating to Bonds or First General Resolution Bonds which provides that during the term of such agreement the Authority is to pay to the Counterparty an amount based on the interest accruing at a fixed or variable rate per annum on an amount equal to all or a portion of the principal amount of such Bonds or First General Resolution Bonds and that the Counterparty is to pay to the Authority either (i) an amount

based on the interest accruing on such principal amount at a fixed or variable rate per annum, in each case computed according to a formula set forth in such agreement, or that one shall pay to the other any net amount due under such agreement or (ii) an amount based on the amount by which the rate at which such Bonds or First General Resolution Bonds bear interest exceeds a rate stated in such agreement.

**“Investment Securities”** shall mean and include any of the following securities, if and to the extent the same are at the time legal investments by the Authority of the funds to be invested therein and conform to the policies set forth in any investment guidelines adopted by the Authority and in effect at the time of the making of such investment:

(i) direct obligations of, or obligations guaranteed as to principal and interest by, the State or direct obligations of any agency or public authority thereof, provided such obligations are rated, at the time of purchase, in one of the two highest rating categories by each Rating Agency then maintaining a rating on Outstanding Bonds;

(ii) (a) any bonds or other obligations which as to principal and interest constitute direct obligations of, or are guaranteed by the United States of America, including obligations of any agency thereof or corporation which has been or may hereafter be created pursuant to an Act of Congress as an agency or instrumentality of the United States of America to the extent unconditionally guaranteed by the United States of America or (b) any other receipt, certificate or other evidence of an ownership interest in obligations or in specified portions thereof (which may consist of specified portions of the interest thereon) of the character described in subclause (a) of this clause (ii);

(iii) obligations of any agency, subdivision, department, division or instrumentality of the United States of America; or obligations fully guaranteed as to interest and principal by any agency, subdivision, department, division or instrumentality of the United States of America;

(iv) banker’s acceptances or certificates of deposit issued by a commercial bank (a) whose long-term debt obligations are rated by each Rating Agency then maintaining a rating on the Outstanding Bonds at least equal to the rating on Outstanding Bonds that are not insured or otherwise secured by a Credit Facility or a Special Credit Facility, (b) that has its principal place of business within the State and (c) that has capital and surplus of more than \$100,000,000;

(v) corporate securities, including commercial paper and fixed income obligations, which are, at the time of purchase, rated by each Rating Agency then maintaining a rating on Outstanding Bonds, in its highest rating category for comparable types of obligations;

(vi) repurchase agreements collateralized by securities described in clause (ii) or (iii) above with any registered broker/dealer or with any domestic commercial bank whose long-term debt obligations are rated “investment grade” by each Rating Agency then maintaining a rating on Outstanding Bonds, provided that (a) a specific written repurchase agreement governs the transaction, (b) the securities are held, free and clear of any lien, by the Trustee or an independent third party acting solely as agent for the Trustee, and such third party is either a Federal Reserve Bank or a bank which is a member of the Federal Deposit Insurance Corporation and which has combined capital, surplus and undivided profits of not less than \$25 million, and the Trustee shall have received written confirmation from such third party that it holds such securities, free and clear of any lien, as agent for the Trustee, (c) the repurchase agreement has a term of thirty days or less, or the Trustee will value the collateral securities no less frequently than monthly and will liquidate the collateral securities if any deficiency in the required collateral percentage is not restored within five business days of such valuation, (d) the fair market value of the collateral securities in relation to the amount of the repurchase obligation, including principal and interest, is equal to at least 102% and (e) the repurchase agreement meets the guidelines then applicable to such investments of each Rating Agency then maintaining a rating on Outstanding Bonds;

(vii) investment agreements or guaranteed investment contracts with any financial institution whose prior long term debt obligations, or whose obligations under such an investment agreement or



guaranteed investment contract, are guaranteed by a financial institution whose senior long term debt obligations, have a rating (at the time such agreement or contract is entered into) in one of the two highest rating categories or comparable types of obligations by each Rating Agency then maintaining a rating on the Bonds;

(viii) money market funds rated in the highest rating category for comparable types of obligations by each Rating Agency then maintaining a rating on the Bonds; and

(ix) municipal obligations, the payment of principal and redemption price, if any, and interest on which is irrevocably secured by obligations of the type referred to in clauses (i), (ii) or (iii) above and which obligations have been deposited in an escrow arrangement which is irrevocably pledged to the payment of such municipal obligations and which municipal obligations are rated in the highest rating category for comparable types of obligations by each Rating Agency then maintaining a rating on the Bonds.

Obligations of the Trustee or an affiliate thereof may be Investment Securities, provided that they otherwise qualify.

**“Local Water Fund”** shall mean the special fund by that name established by the Act in the custody of the Board.

**“Mayor”** shall mean the Mayor of the City or such other person duly appointed and authorized to act on behalf of the Mayor.

**“Monthly Balance”** shall mean the amount, calculated as of the first day of each month, equal to the sum of:

(i) For the Bonds of a Series and Parity Reimbursement Obligations which are Outstanding during the Fiscal Year in which such month falls, an amount equal to the product obtained by multiplying (a) the difference between (1) the amount of interest due or projected to be due on or prior to the later of the next Succeeding Bond Payment Date for such Bonds and the 15th day of the next succeeding month and (2) the amount, if any, held in the sub-account for such Bonds in the Capitalized Interest Account by (b) a fraction, the numerator of which is the number of full months since the end of the month preceding the last Bond Payment Date for such Bonds (or, with respect to the first Bond Payment Date for such Bonds, the number of full months since the last day of the month preceding the date of issuance of such Bonds) and the denominator of which is the number of months between Bond Payment Dates for such Bonds minus one (or, with respect to the first Bond Payment Date therefor, the number of months between the last day of the month preceding the date of issuance of such Bonds and the first Bond Payment Date therefor minus one); *provided, however*, that if this formula would produce (A) a fraction greater than one, then the fraction shall be equal to one, or (B) a denominator less than one, then the fraction shall equal one; plus

(ii) For the Bonds of a Series and Parity Reimbursement Obligations which are Outstanding during the Fiscal Year in which such month falls, an amount equal to the Principal Installment due on the next Succeeding Bond Payment Date, which falls within twelve months or less, on which a Principal Installment on such Bonds is due, multiplied by a fraction, the numerator of which is the number of full months since the last day of the month preceding the last Bond Payment Date on which a Principal Installment on such Bonds was due (or, with respect to the first such Bond Payment Date, twelve minus the number of full months to the first Bond Payment Date on which a Principal Installment on such Bonds is due), and the denominator of which is eleven; *provided, however*, that if this formula would produce a fraction greater than one, then the fraction shall be equal to one; plus

(iii) For Parity Bond Anticipation Notes which are outstanding during the Fiscal Year in which such month falls, an amount equal to the product obtained by multiplying (a) the difference between (1) the amount of interest due or projected to be due during such Fiscal Year on such Parity Bond Anticipation Notes and (2) the amount, if any, held in the sub-account for such Parity Bond Anticipation Notes in the Capitalized Interest Account, by (b) a fraction, the numerator of which is the number of full months since the end of the month preceding the last interest payment date for

such Parity Bond Anticipation Notes (or, with respect to the first interest payment date for such Parity Bond Anticipation Notes, the number of full months since the last day of the month preceding the date of issuance of such Parity Bond Anticipation Notes) and the denominator of which is the number of months between interest payment dates for such Parity Bond Anticipation Notes minus one (or, with respect to the first interest payment date for such Parity Bond Anticipation Notes, the number of months between the last day of the month preceding the date of issuance of such Parity Bond Anticipation Notes and the first interest payment date therefor minus one); *provided, however*, that if this formula would produce (A) a fraction greater than one, then the fraction shall be equal to one, or (B) a denominator less than one, then the fraction shall equal one.

**“Operating Expenses”** shall have the meaning ascribed thereto in the Agreement.

**“Option Bonds”** shall mean Bonds which by their terms may be tendered by and at the option of the owner whereof for purchase or payment by the Authority prior to the stated maturity thereof, or the maturities of which may be extended by and at the option of the owner thereof.

**“Other Moneys”** shall mean moneys which do not constitute Revenues and which are derived from payments to be made to or upon the order of the Authority (i) by a Counterparty pursuant to an Interest Rate Exchange Agreement relating to First General Resolution Bonds, (ii) by the New York State Environmental Facilities Corporation pursuant to any agreement by and between the Authority and such corporation heretofore or hereafter entered into in connection with the issuance of Bonds or First General Resolution Bonds, including the Loan Agreement, dated as of May 1, 1990, by and between the New York State Environmental Facilities Corporation and the Authority, as amended, the Loan Agreement, dated as of January 1, 1991, by and between the New York State Environmental Facilities Corporation and the Authority, as amended and the Loan Agreement, dated as of December 1, 1991, by and between the New York State Environmental Facilities Corporation and the Authority, as amended, (iii) as Subsidy Payments and (iv) of any other moneys and securities pledged by the Authority to the payment of the Bonds pursuant to Article V of the Resolution and a Supplemental Resolution.

**“Outstanding”** when used with reference to First General Resolution Bonds or Parity Bond Anticipation Notes, shall have the meaning given to such term in the First General Resolution or the resolution pursuant to which such Parity Bond Anticipation Notes were issued, respectively; when used with reference to Parity Reimbursement Obligations, shall have the meaning given to such term in the agreement creating such Parity Reimbursement Obligations; and, when used with reference to Bonds, shall mean, as of any date, all Bonds theretofore or thereupon being authenticated and delivered under the Resolution except:

- (a) any Bonds canceled by the Trustee at or prior to such date;
- (b) any Bond (or portion thereof) for the payment or redemption of which there shall be set aside and held in trust under the Resolution either:
  - (i) moneys in an amount sufficient to pay when due the Principal Installments or Redemption Price thereof, together with all accrued interest,
  - (ii) Defeasance Obligations in such principal amounts, of such maturities, bearing such interest and otherwise having such terms and qualifications, as are necessary to provide moneys (whether as principal or interest) in an amount sufficient to pay when due the Principal Installments or Redemption Price thereof, together with all accrued interest, or
  - (iii) any combination of (i) and (ii) above,

and, if such Bond or portion thereof is to be redeemed, for which notice of redemption has been given as provided in Article VI, or the applicable Supplemental Resolution, or provision satisfactory to the Trustee has been made for the giving of such notice;

- (c) any Bond in lieu of or in substitution for which other Bonds have been authenticated and delivered; and
- (d) any Bond deemed to have been paid as provided in Section 1201(b) of the Resolution.

**“Parity Bond Anticipation Note”** shall mean a Bond Anticipation Note the interest on which is payable from and secured by a pledge of, and lien on, Revenues, Other Moneys and amounts on deposit in the FGR Subordinated Indebtedness Fund on a parity with the lien created by Section 501 of the Resolution.

**“Parity Reimbursement Obligation”** shall mean a Reimbursement Obligation, the payment of which is secured by a pledge of, and a lien on, Revenues, Other Moneys and amounts on deposit in the FGR Subordinated Indebtedness Fund on a parity with the lien created by Section 501 of the Resolution.

**“Principal Installment”** shall mean, as of any date of calculation and with respect to any Series, so long any Bonds thereof are Outstanding, (i) the principal amount of Bonds (including (x) any amount designated in, or determined pursuant to, the applicable Supplemental Resolution, as the “principal amount” with respect to any Bonds which do not pay full current interest for all or any part of their term, (y) the Tender Option Price of any Option Bonds which may be tendered to the Authority for purchase or payment prior to the stated maturity thereof in accordance with the terms of the Supplemental Resolution authorizing such Option Bonds, unless such amount is secured by a Credit Facility which is not in default and (z) the principal amount of any Parity Reimbursement Obligation) of such Series due (or so tendered for purchase or payment) on a certain future date for which no Sinking Fund Installments have been established, or (ii) the unsatisfied balance of any Sinking Fund Installments due on a certain future date for Bonds of such Series, or (iii) if such future dates coincide as to different Bonds of such Series, the sum of such principal amount of Bonds and of such unsatisfied balance of Sinking Fund Installments due on such future date.

**“Projected Debt Service”** for any Fiscal Year or part thereof shall mean, unless used in relation to First General Resolution Bonds, an amount with respect to a Projected Series, certified by the Authority to the Trustee and the Board, as provided in the Agreement, equal to the Debt Service estimated by the Authority to be payable during such Fiscal Year or part thereof on such Projected Series, and, when used in relation to First General Resolution Bonds, shall have the meaning ascribed thereto in the First General Resolution.

**“Projected Series of Bonds”** or **“Projected Series”** shall mean any Series of Bonds or Parity Bond Anticipation Notes described in an Authority Budget as anticipated to be issued in the Fiscal Year to which such Authority Budget relates.

**“Rating Agency”** shall mean each of Moody’s Investors Service and Standard & Poor’s Ratings Services and its respective successors and assigns.

**“Redemption Price”** shall mean, when used with respect to a Bond or portion thereof, the principal amount thereof plus the applicable premium, if any, payable upon either optional or mandatory redemption thereof pursuant to the Resolution.

**“Refunding Bond”** shall mean any Bond authenticated and delivered on original issuance pursuant to the Resolution for the purpose of refunding any Outstanding Bonds, or thereafter authenticated and delivered pursuant to the Resolution in lieu of or substitution for such Bond.

**“Reimbursement Obligation”** shall mean the obligation of the Authority described in the Resolution (i) to reimburse directly the issuer of a Credit Facility for amounts paid by such issuer thereunder or (ii) make payment to a Counterparty of amounts payable thereto by the Authority pursuant to an Interest Rate Exchange Agreement relating to Bonds, in either case.

**“Required Deposits”** shall mean, for any Fiscal Year during which First General Resolution Bonds are Outstanding, the amount, if any, payable into the FGR Authority Expense Fund, the FGR Debt Service Reserve Fund and the FGR Subordinated Indebtedness Fund, and for any Fiscal Year during which no First General Resolution Bonds are Outstanding, the amount, if any, payable into the Authority Expense Fund, the Debt Service Reserve Fund and the Subordinated Indebtedness Fund, but in each case only to the extent such payments are required to be made from Revenues.

**“Resolution”** shall mean the Water and Sewer System Second General Revenue Bond Resolution, adopted by the Authority on March 30, 1994, as the same may be amended or supplemented by a Supplemental Resolution.

**“Revenue Fund”** shall mean the fund by that name established pursuant to the Resolution.

**“Revenues”** shall have the meaning given to it in the Agreement as the same may be amended from time to time in accordance therewith and the Resolution.

**“Series”** or **“Series of Bonds”** shall mean all of the Bonds authenticated and delivered on original issuance identified pursuant to the Supplemental Resolution authorizing such Bonds as a separate Series of Bonds and any Bonds thereafter authenticated and delivered in lieu of or in substitution therefor pursuant to the Resolution regardless of variations in maturity, interest rate or other provisions.

**“SGR Cash Flow Requirement”** shall mean, for each Fiscal Year and as of any date of certification, the amount of Revenues, certified by the Authority to the Trustee and the Board as provided in the Agreement and the Resolution, to be required to be deposited into the Subordinated Indebtedness Fund in such Fiscal Year, which amount shall be equal to the difference between (a) the sum of (i) the Aggregate Debt Service for such Fiscal Year, (ii) the Projected Debt Service for such Fiscal Year, (iii) the amount of Parity Reimbursement Obligations payable in such Fiscal Year, (iv) the amount, if any, required to restore the Debt Service Reserve Fund to the Debt Service Reserve Requirement and (v) the amount, if any, withdrawn from the Construction Account pursuant to the First General Resolution during such or any prior Fiscal Year and (b) the sum of (i) if such certification is made prior to the commencement of such Fiscal Year, the amount anticipated by the Authority as of such date of certification to be held, as of the first day of such Fiscal Year, in the Revenue Fund or (ii) if such certification is made after the commencement of such Fiscal Year, the amount held, as of the first day of such Fiscal Year, in the Revenue Fund and (iii) the amount of Other Moneys paid or projected to be paid to the Authority during such Fiscal Year.

**“Sinking Fund Installment”** shall mean, as of any particular date of calculation, the amount required, as of such date of calculation, to be paid by the Authority on a future date for the retirement of Outstanding Bonds which are stated to mature subsequent to such future date, but does not include any amount payable by the Authority by reason only of the maturity of a Bond.

**“Special Account”** shall mean one or more of the Special Accounts established in the Debt Service Reserve Fund by a Supplemental Resolution pursuant to the Resolution.

**“Special Credit Facility”** shall mean, with respect to any Series of Bonds or portion thereof, a Credit Facility (a) which provides funds for (i) the direct payment of the Principal Installments of and interest on such Bonds when due or (ii) the payment of the Principal Installments of and interest on such Bonds in the event amounts otherwise pledged to the payment thereof are not available when due or (iii) the payment of the Tender Option Price of any Option Bond which may be tendered to the Authority for purchase or payment in accordance with the Supplemental Resolution authorizing such Option Bond (in any case, regardless of whether such Credit Facility provides funds for any other purpose) and (b) which (i) requires the Authority to reimburse the issuer of such Credit Facility directly for amounts paid thereunder and (ii) provides that such obligation is a Parity Reimbursement Obligation.

**“State”** shall mean the State of New York.

**“Subordinated Indebtedness”** shall mean any bond, note or other evidence of indebtedness issued by the Authority in furtherance of its corporate purposes under the Act and secured by a pledge of moneys in the Subordinated Indebtedness Fund or Other Moneys, or both, which is subordinate to the pledge thereof made under the Resolution.

**“Subordinated Indebtedness Fund”** shall mean the fund by that name established pursuant to the Resolution.

**“Subsidy Payments”** shall mean amounts payable to the Authority by the United States of America or by the State or by any agency or instrumentality of either in connection with Bonds of the Authority which amounts do not constitute Other Moneys described in the paragraph (ii) of the definition of Other Moneys.

**“Supplemental Resolution”** shall mean a resolution of the Authority authorizing the issuance of a Series Bonds or otherwise amending or supplementing the Resolution, adopted in accordance with Article VIII of the Resolution.

“**Surplus Fund**” shall mean the fund by that name established pursuant to the Resolution.

“**System**” shall mean the “Water System” and the “Sewer System” as such quoted terms are defined in Sections 1045-b(14) and (21) of the Act.

“**Tender Option Price**” shall mean, with respect to any Option Bond tendered for purchase or payment in accordance with the Supplemental Resolution authorizing such Option Bond, an amount equal to the principal amount of such Option Bond plus the interest accrued and unpaid thereon to the date of such tender.

“**Trustee**” shall mean United States Trust Company of New York, and its successor or successors and any other person which may at any time be substituted in its place pursuant to the Resolution.

“**Variable Rate Bond**” shall mean, as of any date of determination, any Bond on which the interest rate borne thereby may vary during any part of its remaining term.

“**Water Project**” shall have the meaning ascribed thereto in Section 1045-b(20) of the Act, including any sewerage facility, water facility or water and sewerage facility as described therein and constituting a part of the System.

### **Summary of Certain Documents**

The following are brief summaries of certain provisions of the Agreement, the Lease, the Authority General Resolution and the Second Resolution. These summaries do not purport to be complete and are subject in all respects to the provisions of, and are qualified in their entirety by, reference to the respective documents to which they relate.

### **Summary of the Agreement**

**Financing of Water Projects.** The Authority agrees to use its best efforts to finance all or a part of the Cost of all Water Projects described in Appendix A to the Agreement. In consideration for the Authority’s issuance of the Bonds, the Board gives, grants, conveys and transfers to the Authority all of its right, title and interest in the Revenues, including without limitation, all of its rights to collect and receive said Revenues subject only to provisions of the Act, the Agreement and the Resolution permitting the application of said Revenues to the purposes therein set forth. The Board itself incurs no indebtedness under the terms of the Agreement, Lease, Resolution or any other document executed in connection therewith. *(Sections 2.1, 2.2 and 2.4)*

**Transfer of Funds.** The Authority shall deposit the proceeds of each Series of Bonds with the Trustee in accordance with the provisions of the Resolution and the Supplemental Resolution authorizing such Series; provided, however, that the portion of the proceeds designated to pay the Costs of any Water Project shall be held only in the Construction Fund established pursuant to the Resolution.

The Authority shall authorize payment of such Costs in the manner set forth in the Resolution once evidence thereof is provided in a Certificate signed by an Authorized Representative of the Board or City, as the case may be. Neither the Authority nor the Trustee shall be required to provide funds to pay the Costs of Water Projects from any source other than the Construction Fund, and neither the Authority nor the Trustee shall pay to the City from such Fund any amount in excess of that set aside for the purposes thereof, or for the Projects listed in Appendix A to the Agreement. *(Sections 3.1 and 3.2)*

**Local Water Fund.** The Board shall deposit all Revenues, as promptly as practicable after receipt, into the Local Water Fund. There shall also be deposited in the Local Water Fund all amounts received by the Board from the Trustee pursuant to the Resolution. *(Section 4.1)*

**Establishment of Certain Funds and Application of Revenues in Local Water Fund.** The Board shall establish two special funds (in addition to the Local Water Fund) to be held by the Board at a Depository: the Board Expense Fund and the Operation and Maintenance Reserve Fund, with the General Account therein. The Board shall hold such funds as trust funds and the amounts on deposit shall only be applied for the purposes provided in the Agreement.

Beginning on the first day of each month in each Fiscal Year, the Board is required to apply the Revenues in the Local Water Fund, *first*, to the Trustee for deposit in the Revenue Fund until the amount on deposit in the Revenue Fund equals the Minimum Monthly Balance for such month and the Trustee shall have received the amounts, if any, required to be deposited in the Authority Expense Fund, the Debt Service Reserve Fund and the Subordinated Indebtedness Fund for such month. Thereafter, in such month from the balance remaining in the Local Water Fund, the Board is required, after making provision for Board Expenses, to pay to the City  $\frac{1}{12}$ th of the operating expenses for such Fiscal Year. After making such payments, any amounts remaining in the Local Water Fund in each month are applied daily (i) to satisfy the Cash Flow Requirement (if the required payments to the City for Operating Expenses have been made), (ii) to satisfy required payments to the City for Operating Expenses (if the Cash Flow Requirement has been satisfied) or (iii) proportionately, to the Trustee for deposit in the Revenue Fund and to the City for the payment of Operating Expenses, until the total of all amounts deposited in the Revenue Fund during such Fiscal Year equals the Cash Flow Requirement and all Operating Expenses required to be paid shall have been paid. Thereafter, as long as the amount on deposit in the Revenue Fund in each month is equal to the Minimum Monthly Balance and the Cash Flow Requirement continues to be met, all such amounts in the Local Water Fund shall be paid as follows: *first*, to the Authority until the total of the amounts so paid equals the principal of and interest on any bonds, notes or other obligations of the Authority (other than Bonds, Bond Anticipation Notes, and Subordinated Indebtedness) payable within the then current Fiscal Year, together with all other amounts necessary to make the required deposits to the reserve and other funds and amounts established for such bonds, notes or other obligations; *second*, to the City until the amounts so paid are equal to the rental payment for such Fiscal Year and the unsatisfied balance, if any, of the rental payment for any prior Fiscal Year; and, *third*, to the Operation and Maintenance Reserve Fund, until the amount therein on deposit is equal to the O&M Reserve Requirement for such Fiscal Year. Any amounts remaining in the Local Water Fund on the last day of each Fiscal Year shall be paid to the General Account in the Operation and Maintenance Reserve Fund. (Section 4.2)

**Minimum Monthly Balance.** The Minimum Monthly Balance shall be calculated as of the first day of the month and shall be equal to the sum of:

(i) For each Series of Bonds which is Outstanding during the current Fiscal Year, an amount equal to the product obtained by multiplying (a) the difference between (1) the amount of interest due or projected to be due on the next succeeding Bond Payment Date for such Series and (2) the amount, if any, held in the applicable subaccount for such Series in the Capitalized Interest Account in the Debt Service Fund by (b) a fraction, the numerator of which is the number of full months since the end of the month preceding the last Bond Payment Date for such Series (or, with respect to the first Bond Payment Date for such Series, the number of full months since the last day of the month preceding the date of issuance of such Series) and the denominator of which is the number of months between Bond Payment Dates minus one (or, with respect to the first Bond Payment Date for a Series, the number of months between the last day of the month preceding the date of issuance of such Series and the first Bond Payment Date minus one); provided, however, that if this formula would produce (A) a fraction greater than one, then the fraction shall be equal to one, or (B) a denominator less than one, then the fraction shall be equal to one; plus

(ii) For each Series of Bonds which is Outstanding during the current Fiscal Year, an amount equal to the Principal Installment due or projected to be due on the next succeeding Bond Payment Date for such Series which falls within twelve months or less on which a Principal Installment is due, multiplied by a fraction, the numerator of which is the number of full months since the last day of the month preceding the last Bond Payment Date on which a Principal Installment was due (or, with respect to the first such Bond Payment Date, twelve minus the number of full months to the first Bond Payment Date on which a Principal Installment is due), and the denominator of which is eleven; provided, however, that if this formula would produce a fraction greater than one, then the fraction shall be equal to one. (Section 4.3)

**Deposits to Operation and Maintenance Reserve Fund.** There shall be deposited to the Operation and Maintenance Reserve Fund in each Fiscal Year from the sources described below the amount required, if any, so that the amounts on deposit therein satisfy the O&M Reserve Fund Requirement for the ensuing Fiscal Year.

Deposits to the Operation and Maintenance Reserve Fund may be made from the proceeds of the sale of Bonds of the Authority, from the Local Water Fund, or from any other moneys lawfully available therefor, subject to the following limitations:

(i) The maximum deposit to the Operation and Maintenance Reserve Fund from the proceeds of Bonds of the Authority, as of any time of calculation, may not exceed the O&M Reserve Fund Requirement then in effect, reduced by the cumulative sum of prior deposits thereto from proceeds of Bonds of the Authority.

(ii) Deposits to the Operation and Maintenance Reserve Fund from the Local Water Fund shall be subject to the priorities established in Section 4.2 of the Agreement.

(iii) If there shall be a deficit in the Operation and Maintenance Reserve Fund on May 1 of any Fiscal Year, and if as of such May 1 the Board does not project that available Revenues will at least equal the O&M Reserve Requirement for such Fiscal Year by June 30 of such Fiscal Year, then the Board shall include in its Annual Budget for the ensuing Fiscal Year an amount sufficient, together with other amounts available therefor, to at least equal the O&M Reserve Fund Requirement for the ensuing Fiscal Year.

If on July 1 of any Fiscal Year the amount on deposit in the Operation and Maintenance Reserve Fund is less than the O&M Reserve Fund Requirement, such deficit shall (subject to paragraph (i) above) be made up from the proceeds of the sale of Bonds issued during such Fiscal Year; provided, however, if, prior to May 1 of such Fiscal Year such deficit has not been made up from Bond proceeds, the Board shall include the amount of such deficit in its Annual Budget for the ensuing Fiscal Year and the amounts necessary to restore such deficit shall be deposited in the Operation and Maintenance Reserve Fund.

Amounts required to be deposited in the General Account shall be held separate and apart from other amounts held in the Operation and Maintenance Reserve Fund and applied as described below. *(Section 4.4)*

**Application of Moneys in the Operation and Maintenance Reserve Fund.** If on the first day of any month the Board has not paid to the City an amount equal to the product of (i) the amount required to be paid for Operating Expenses pursuant to Section 8.1 of the Lease, multiplied by (ii) a fraction the numerator of which is the number of months which have commenced during such Fiscal Year, and the denominator of which is 12, the Board shall withdraw from the Operation and Maintenance Reserve Fund and pay to the City, on demand, an amount equal to  $\frac{1}{12}$  of the amount so required to be paid pursuant to Section 8.1 of the Lease, or the entire balance in such Fund if less than sufficient. Amounts on deposit in the General Account may be applied (i) to purposes provided for in Section 4.2, (ii) to the payment of Bonds in accordance with Article XII of the Resolution or (iii) to the Costs of Water Projects, but shall be retained therein to the extent required by the Annual Budget. *(Section 4.5)*

**Application of Moneys in Board Expense Fund.** Amounts on deposit in the Board Expense Fund shall be applied by the Board solely for the purposes of paying expenses of the Board, in accordance with the Annual Budget. *(Section 4.6)*

**Application of Revenues After Default.** The Board has covenanted that if an “event of default” (as defined in the Resolution) shall occur, the Board shall pay or cause to be paid to the Trustee, upon its request, all moneys and securities then held by the Board in the Local Water Fund and thereafter the Revenues as promptly as practicable after receipt. *(Section 4.7)*

**Amounts Remaining.** Any amounts received or held by the Authority or the Trustee pursuant to the Resolution, any similar document or the Agreement after all Bonds and other evidences of indebtedness have been paid in full or are no longer Outstanding and after payment of all other obligations and expenses of the Authority, or provision for payment thereof has been made, shall be paid to the City.

Any payments by the City to the Water Board pursuant to Section 1045-h(3) of the Act shall be confined to consideration for the sale of goods or the rendering of services by the Water Board to the City pursuant to the Lease or the Agreement as contemplated by the Act. *(Section 4.8)*

**Rate Covenant.** The Board has covenanted and agreed to establish, fix and revise fees, rates or other charges for the use of or services furnished by the System which, together with any other available funds, are adequate to provide for (i) the timely payment of the Principal Installments of and interest on all Bonds and the principal of and interest on any other indebtedness of the Authority payable from Revenues, (ii) the proper operation and maintenance of the System, (iii) all other payments required for the System not otherwise provided for and (iv) all other payments required pursuant to the Agreement and the Lease. Without intending to limit the generality of the foregoing, the Board has also covenanted to establish and collect rates, fees and charges sufficient in each Fiscal Year so that Revenues collected in such Fiscal Year will be at least equal to the sum of (i) 115% of estimated Aggregate Debt Service and Projected Debt Service payable in such Fiscal Year (excluding any Refundable Principal Installment if payable from funds held in trust therefor and assuming with respect to Variable Rate Bonds that the effective rate of interest is that which the Authority determines so long as such rate is not less than the rate such Bonds bear at the time Aggregate Debt Service is determined), (ii) 100% of the Operating Expenses and Authority Expenses payable in such Fiscal Year and (iii) 100% of the amount necessary to pay the other Required Deposits for such Fiscal Year. However, a failure to generate such Revenues does not constitute an “event of default” if the Board takes timely action to correct any such deficit. The Board shall review, at least annually, such rates, fees and charges to determine whether such rates, fees and charges are, or will be, sufficient to meet the requirements thereof and shall promptly take action to cure or avoid any deficiency. Except to the extent required by Section 1045-j of the Act, as in effect on July 24, 1984, with regard to the requirement that tax exempt organizations be charged for service provided by the System or by existing agreements (including any successor agreements with Jamaica Water), the Board will not furnish or supply any product, use or service of the System free of charge or at a nominal charge. *(Section 6.1)*

**Consulting Engineer and Rate Consultant.** The Authority shall employ a Consulting Engineer and a Rate Consultant whose duties, respectively, shall be to make any certificates and perform any other acts required or permitted of the Consulting Engineer and the Rate Consultant under the Agreement and the Resolution. If so determined by the Authority, the same person or firm may perform the duties and functions of the Consulting Engineer and the Rate Consultant.

In each Fiscal Year, the Consulting Engineer and the Rate Consultant shall make an examination of, and shall report to the Authority, the Board, the City and the Trustee, on the properties and operations of the System. The report of the Rate Consultant shall set forth among other findings, the Rate Consultant’s recommendation as to any necessary or advisable revisions of rates, fees and charges for the ensuing Fiscal Year and such other advice and recommendation as it may deem desirable. The Consulting Engineer’s report shall set forth its findings as to whether the System has been maintained in good repair and sound operating condition, and its estimate of the amount, if any, required to be expended to place such properties in such condition and the details of such expenditures and the approximate time required therefor. The City covenants that if any such report of the Consulting Engineer shall set forth that the properties of the System have not been maintained in good repair and sound operating condition, it will promptly restore the properties to good repair and sound operating condition with all expedition practicable. *(Section 6.2)*

**Covenant to Operate and Maintain System.** The City has covenanted that it shall, at all times:

(a) in accordance with the advice and recommendations of the Consulting Engineer, operate the System properly and in a sound and economical manner and maintain, preserve, and keep the same preserved and kept with the appurtenances and every part and parcel thereof, in good repair, working order and condition, and from time to time make, or cause to be made, all necessary and proper repairs, replacements and renewals so that at all times the operation of the System may be properly and advantageously conducted, regardless of any failure on the part of the Board to make the payments to the City required by Section 8.1 of the Lease; provided, however, that nothing contained in the Agreement shall require the City to operate, maintain, preserve, repair, replace, renew or reconstruct any part of the System if there shall be filed with the Board, the Authority and the Trustee (i) a certificate of the Commissioner acting as the Authorized Representative of the City stating that in the opinion of the City abandonment of operation of such part of the System will not



adversely affect the operation of the System or the amount of Revenues derived therefrom and is not prejudicial to the interests of the Board, the Authority or the Bondholders and (ii) a Certificate of the Consulting Engineer concurring with such statement;

(b) enforce the rules and regulations governing the operation, use and services of the System established from time to time by the Board or the City;

(c) observe and perform all of the terms and conditions contained in the Act, and comply with all valid acts, rules, regulations, orders and directions of any legislative, executive, administrative or judicial body having competent jurisdiction of the City or the System; provided, however, that the failure of the City to comply with the covenant contained in this subsection (c) for any period shall not constitute a default on its part so long as the City (i) is taking reasonable and timely steps to permit compliance and (ii) the City shall have delivered to the Board and to the Authority a Certificate of the Consulting Engineer which (1) sets forth in reasonable detail the facts and circumstances attendant to such non-compliance, (2) sets forth the steps being taken by the City to permit compliance, (3) sets forth the estimated date on which the City will be in compliance and (4) states that in the opinion of the Consulting Engineer such non-compliance during the period described will not adversely affect the operation of the System or the amount of Revenues to be derived therefrom; and

(d) not create or suffer to be created any lien or charge upon the System or any part thereof except for Permitted Encumbrances. (*Section 6.3*)

**Annual Budget.** On May 1 of each year (or on such later date as the Authority, the Board and the City may agree) the Authority shall deliver to the Board a certified copy of the Authority Budget for the ensuing Fiscal Year showing the Cash Flow Requirement for such Fiscal Year. Based upon the information contained in (a) the Authority Budget, (b) the City's certification pursuant to Section 8.3 of the Lease and (c) the Certificate of the Consulting Engineer delivered to the Board pursuant to Section 8.3 of the Lease (collectively, the "Budget Documents"), the Board shall prepare the Annual Budget for the ensuing Fiscal Year. In addition to the information contained in the Budget Documents the Board shall also make provision in the Annual Budget for Board Expenses for the ensuing Fiscal Year, for the amount, if any, required to be deposited in the Operation and Maintenance Reserve Fund in accordance with Section 4.4 of the Agreement, and for the application of the amounts in the General Account therein. Thereafter, but in no event later than 15 days after the date of publication of the Executive Budget of the City, the Board shall adopt such Annual Budget. Promptly after adoption of the Annual Budget, and in no event later than June 10 (or such other date as the Authority, the Board and the City may agree) of each year, the Board shall establish the rates, fees and charges for the use of the System for the ensuing Fiscal Year. The Board may from time to time, either before or after commencement of the Fiscal Year to which it relates, amend the Annual Budget, but (except for its own expenses) only in accordance with and after receipt of amended Budget Documents. If as of the first day of any Fiscal Year an Annual Budget has not been adopted, the Annual Budget for the immediately preceding Fiscal Year shall be the Annual Budget for such Fiscal Year until a new Annual Budget is adopted. (*Section 6.4*)

**Tax Exemption.** The City, the Authority and the Board have covenanted that so long as any Bonds shall be Outstanding, no one will take any action, nor fail to take any action, which, if taken or not taken, as the case may be, would adversely affect the tax-exempt status of the interest payable on the Bonds then Outstanding, the interest on which is excluded from gross income under the Internal Revenue Code of 1986. (*Section 6.5(b)*)

**Discontinuance of Service.** The Board has covenanted to enforce or cause the City to enforce the rules and regulations providing for discontinuance of, or disconnection from, the supply of water or the provision of sewer service, or both, as the case may be, for non-payment of fees, rents, rates or other charges imposed by the Board, provided that such discontinuance or disconnection shall not be carried out except in the manner and upon the notice as is required of a waterworks corporation pursuant to Sections 89(b)(3)(a)-(c) and 116 of the Public Service Law of the State. (*Section 6.7*)

**Covenant of City as to Rates and Charges.** The City has covenanted that, upon the issuance of the Bonds by the Authority, the City will not thereafter levy user fees, rents and other charges with respect

to the System until all Bonds are paid or are no longer Outstanding pursuant to the terms of the Resolution; provided, however, that the City may levy *ad valorem* taxes to pay the costs and expenses of the System or to pay the principal of and interest on any general obligation bonds of the City issued to finance the System or any part thereof. (Section 6.9)

**Books and Records.** Each of the Authority and the Board shall keep or cause to be kept proper books of record and account in which complete and correct entries shall be made of all transactions relating to their corporate purposes under the Act. In accordance with Section 1045-y of the Act, the Authority and the Board shall annually submit to the Mayor, the Comptroller and the Director of Management and Budget of the City a detailed report concerning their activities for the Fiscal Year. In addition, the Authority and the Board shall submit to the Mayor, the Comptroller and the Director of Management and Budget of the City audited annual financial statements of the Authority and the Board together with a report thereon of an accountant satisfactory to the Board. (Section 6.11)

**Liens.** Until the Bonds or other evidences of indebtedness issued by the Authority for its purposes under the Act have been paid in full or provision has been made therefor in accordance with the Resolution or similar document, the Agreement provides that the Board shall not create, and, to the extent it has the power to do so, shall not permit to be created, any lien upon or pledge of the Revenues except the lien and pledge thereon created by the Act. (Section 6.12)

**Security Interests.** Except to the extent provided in the Act, neither the Board nor the Authority may grant any Bondholder any security interest in any of the assets or Properties of the Board. (Section 6.13)

**Financing through State Revolving Fund.** In connection with the financing of Water Projects by the Authority with funds provided from the State Revolving Fund, the City may enter into a Project Financing Agreement or Agreements among DEC, the Corporation and the Authority and make in any such agreement certain representations, warranties, covenants and agreements. (Section 6.16)

**Agreement of the State.** Under the provisions of the Agreement, the parties pledge and agree, for and on behalf of the State as provided in the Act, that the State will not alter or limit the rights vested by the Act in the Authority or the Board to fulfill the terms of any agreement made with or for the benefit of the Bondholders, or in any way impair the rights and remedies of Bondholders, until the Bonds, together with the interest thereon, interest on any unpaid installment of interest, and all costs and expenses incurred in any action or proceeding by or on behalf of such holders, are fully met and discharged. (Section 7.1)

**Events of Default and Remedies.** An “event of default” or a “default” means any one of the following events: (i) failure by the Board to pay the Authority those amounts required under the Agreement; (ii) failure of the City or the Board to observe any covenant, term or condition of the Agreement (other than the payments the Board shall make to the Authority) and such failure shall have continued for a period of sixty (60) days after written notice, specifying such failure and requesting that it be remedied, is given to the City or the Board, or both, by the Authority unless the Authority shall agree in writing to extend such time prior to its expiration, provided such extension shall not be unreasonably withheld if the City or the Board has instituted and is diligently pursuing corrective action which cannot be completed within the applicable period; (iii) the Authority shall file a petition, or otherwise seek relief, under any federal or State bankruptcy or similar law; and (iv) the terms, conditions and security provided under the Agreement and the Resolution or the respective provisions of the Act pursuant to which the Resolution has been adopted or the Bonds have been issued or entered into (including, without limitation, the provisions under which the lien upon the Revenues has been created pursuant to the Agreement and the Resolution and the provisions establishing the powers and obligations of the Board and the relationship of the Authority to the Board and the City) shall be materially and adversely limited, altered or impaired by any legislative action or any final judgment. (Section 8.1)

Whenever an event of default shall have occurred and be continuing, the Authority and the Trustee may take whatever legal action may appear necessary or desirable to: (i) collect the payments then due and as they thereafter become due and (ii) so long as any Bonds are Outstanding, enforce performance

and observance of any obligation or covenant of the City or the Board under the Agreement. In addition, if the Board defaults in making the payments to the Authority required under the Agreement as a result of its failure to impose sufficient fees, rates, rents or other charges, the Authority may petition for the appointment of a receiver to administer the affairs of the Board in order to achieve Revenues sufficient to make such payments by establishing fees, rates, rents or other charges at least sufficient therefor. The remedies conferred upon or reserved to the Authority in respect of any event of default are not exclusive of other available remedies, but shall be in addition to every other remedy given under the Agreement or existing at law or in equity or by statute. (*Sections 8.2 and 8.3*)

**Termination.** The Agreement shall terminate and the covenants and other obligations contained therein shall be discharged and satisfied, when (i) payment of all indebtedness of the Authority has been made or provided for in accordance with the Resolution or similar document securing such indebtedness and (ii) either all payments required thereunder have been made in full, or provision for such payments satisfactory to the Authority has been made, or the City pays or assumes all liabilities, obligations, duties, rights and powers of the Authority under the Agreement. (*Section 9.1*)

**Amendments.** The parties to the Agreement may enter into any amendment, change or modification of the Agreement (if in writing, signed by each of the parties and consented to in writing by the Trustee if required by the Resolution) including, without limitation, amendments to Appendix A to the Agreement; provided that the parties shall enter into no such amendment, change or modification which materially adversely affects the rights of the holders of any Bonds by modifying or revoking certain enumerated provisions of the Agreement without first complying with the applicable provisions of the Resolution. (*Section 10.1*)

**Conflicts.** The Agreement provides that its provisions shall not change or in any manner alter the terms of the Resolution, or the security, rights or remedies of the Trustee or the Bondholders. In the event any provision of the Agreement conflicts at any time, or in any manner, with the provisions of the Resolution or any Bond, the provisions of the Resolution or Bond shall be controlling and conflicting provisions of the Agreement shall be disregarded. (*Section 12.1*)

### **Summary of the Lease**

**Term of Lease and Demise of Leased Property.** The City has leased the Leased Property to the Board for the term of the Lease (the "Lease Term"). The Lease Term commenced on the Effective Date (July 1, 1985) and continues until the later of the 40th anniversary of the Effective Date or the date on which all bonds, notes or other obligations of the Authority are paid in full or provision for such payment is made pursuant to the resolution, trust indenture or other instrument under which such bonds, notes or other obligations are issued. During the Lease Term the Board may use the Leased Property only for its corporate purposes and upon the terms and conditions contained in the Lease.

The Leased Property includes (whether now in use or hereafter acquired, and whether or not located within the boundaries of the City) all of the City's right, title and interest in: (i) the City's sewerage system, including but not limited to all plants, structures, equipment and other real and personal property or rights therein acquired, rehabilitated or constructed (including all work in progress as soon as commenced) and used or to be used for the purpose of collecting, treating, pumping, neutralizing, storing and disposing of sewage, including, but not limited to, main, collecting, outlet or other sewers, pumping stations, groundwater recharge basins, backflow prevention devices, sludge dewatering facilities, vessels, barges, clarifiers, filters and phosphorous removal equipment, vehicles and other property used in connection with the sewer system; (ii) the City's water system, including but not limited to all plants, structures and other real and personal property or rights therein, acquired, rehabilitated or constructed (including all work in progress as soon as commenced) and used or to be used for the purpose of supplying, distributing, accumulating or treating water, including, but not limited to, reservoirs, basins, dams, canals, aqueducts, pipelines, mains, pumping stations, water distribution systems, intake systems, water-works, sources of water supply, purification or filtration plants, water meters and rights of flowage or diversion, vehicles and other property used in connection with the water system; and (iii) any other materials, supplies, plans and property contained in the above-mentioned plants and structures incidental to, or necessary or useful and convenient for, the operation of such facilities; provided, however, that the Leased Property shall not

include the City's right, title and interest in the following: (i) any property or rights of the City the conveyance of which pursuant to the Lease would cause a reversion to or in favor of, or permit a reentry by or in favor of, any third party; (ii) all mines and minerals whatsoever (but not including surface or subsurface waters) now or hereafter found and discovered, crops and timber, on or under the lands to be conveyed pursuant to the Lease; with power and authority for the City to perform certain mineral extraction and agricultural/timber activities; provided, however, that the City shall not undertake any such activities which interfere with the operation, maintenance or collection of Revenues of the System. (Section 2.1)

**Right of City to Enter Leased Property.** The City retains the right to enter upon any portion of the Leased Property, to use any property not constituting a part thereof which is located in, across or upon the Leased Property or for any purpose unless, in the reasonable judgment of the Board, such entry or use would adversely affect the collection of Revenues. (Section 2.2)

**Substitution of Board for City.** Where necessary or desirable and to the extent permitted by law, the City and the Board agree to use their best efforts to substitute the Board for the City with respect to any application or proceedings filed or commenced in relation to the Leased Property with the various State and federal regulatory bodies having jurisdiction. (Section 2.5)

**Indemnification.** The City agrees, to the extent permitted by law and subject to certain conditions, to hold the Board harmless from any and all liability, loss or damage from or in connection with any act the Board does or omits in the exercise of its powers if taken or omitted in good faith and in pursuance of its corporate purposes. (Sections 3.1, 3.2 and 7.2)

**Operation and Maintenance of the Leased Property.** The City shall administer and operate the Leased Property, maintain the Leased Property in good and safe order and condition and make all repairs therein. The City's duty to "maintain" and "repair" shall include all necessary repairs, replacements, renewals, alterations and additions, whether structural, non-structural, ordinary or extraordinary and its duty to "administer" shall include, without limitation, the enforcement of regulations of the Board and the City relating to the use of the System. However, the Lease shall not impose any obligation or liability upon the City for the administration, operation, maintenance and repair of the System not previously imposed upon it in connection with its prior operation and maintenance of the System. Both the Board and the City shall use all reasonable care to prevent the occurrence of waste, damage or injury to the Leased Property. The System shall be used and operated and maintained in accordance with all applicable laws, rules and regulations. (Sections 4.1, 4.2 and 4.3)

**Construction and Acquisition.** The Board authorizes the City to perform the construction and effectuation of any Water Project specified in the Agreement and the City may incur Costs in connection therewith. The City may acquire all real and personal property, or any interest therein, necessary or useful for the construction or effectuation of a Water Project; provided that all such property or interest acquired by the City through the exercise of the power of eminent domain shall be taken in the name of the City. (Sections 5.1, 5.2 and 5.3)

**Billing and the Levy of Water and Sewer Charges.** The City has agreed to provide billing services to the Board. Such services include but are not limited to: (i) notification to users of the System of the water and sewer charges levied by the Board, (ii) collection of such charges (including the City's use of its power of enforcement and collection of unpaid taxes under the laws of the State to enforce and collect any delinquent water and sewer charges from the persons and property liable therefor) and (iii) maintenance of the books, records and accounts of the billing systems. (Sections 6.1 and 6.2)

**Late Payments.** All late payments of water and sewer charges are the property of the Board and shall be collected by the City on behalf of the Board. Notwithstanding the foregoing, the Board has assigned to the City all of its rights and interest in and to all outstanding charges levied and uncollected on all properties at the time title thereto is vested in the City pursuant to *in rem* proceedings in consideration for the City's payment to the Board, in each Fiscal Year after the Effective Date, of an amount equal to 2% of such outstanding charges (unless, during the Lease Term, the City and the Board mutually agree on a different procedure for allocating such outstanding charges). (Section 6.3)

**Discontinuance of Billing Services.** If either the City or the Board no longer desires that the City provide the Board with billing services, the party desiring termination shall give written notice of such fact to the other party at least two years prior to the termination. Notwithstanding such termination of billing services, Section 6.2 of the Lease shall remain in full force and effect. (*Section 6.4*)

**Legal Services.** The Board has hired the City's Law Department to provide it with legal services. However, the Board may hire a different attorney or firm of attorneys to provide it with legal services. If the Board retains counsel to defend a claim against it without the prior approval of the Corporation Counsel of the City (which approval shall not be unreasonably withheld), the Board shall not be entitled to the indemnification from the City provided in Article III of the Lease with respect to such claim, unless the City elects in writing to provide such indemnification. (*Sections 7.1 and 7.2*)

**Payments of Costs by the Board.** The Board has agreed to pay to the City amounts sufficient to: (i) pay the cost of administration, maintenance, repair and operation of the Leased Property, including overhead costs incurred by the City attributable to the Leased Property (but less the amount of any governmental operating aid received or receivable within the current Fiscal Year with respect to the System), the cost of materials and supplies, and the amount of any judgment or settlement paid by the City arising out of a tort claim (but only if the costs of such claim are not otherwise reimbursed, the City's liability for such claim is related to Construction of a Water Project or operation or maintenance of the System and the costs of such claims do not exceed for any Fiscal Year 5% of the aggregate revenues shown on the Board's last year-end audited financial statements); (ii) reimburse the City for capital Costs incurred by the City in the Construction of Water Projects (if requested by the City and not otherwise reimbursed) including, without limitation, the payment of any judgment or settlement arising out of a contract claim related to the Construction of any Water Project; (iii) pay the cost of billing and collection services provided by the City; (iv) pay the cost of legal services provided by the City; and (v) reimburse the City for the compensation, or the costs of the services, of any City officers and employees provided on a full-time or part-time basis to the Board. (*Section 8.1*)

**Base Rental Payments.** In addition, the Board shall pay the City a rental payment for the System, but only to the extent requested by the City, and not to exceed the greater of (i) the principal and interest payable on general obligation bonds issued by the City for water and sewer purposes and certified by the City to be paid within such Fiscal Year, or (ii) 15% of the amount of principal and interest payable on the Bonds of the Authority and certified by the Authority to be paid within such Fiscal Year. (*Section 8.2*)

**Method of Payment.** The City shall certify within five business days after publication of the City's Executive Budget for the ensuing Fiscal Year the (i) amount which the City reasonably anticipates it will expend in connection with the costs described in Section 8.2 of the Lease and (ii) the amount of the payments described in Section 8.1 of the Lease; provided that, prior to the Board's payment to the City the Board shall have received, in addition to such certification by the City, a certificate of the Consulting Engineer to the effect that such amounts certified by the City for such payments and costs are reasonable and appropriate. Upon the Board's payment of all such amounts so certified or requested and any other payments required under the Act, or, after provisions for their payment have been made, the Board shall pay to the City, as Additional Rent in each Fiscal Year, any surplus of funds received. (*Section 8.3*)

**Disposition of Property.** The Board agrees that it will not sell, lease, sublease, assign, transfer, encumber (other than Permitted Encumbrances) or otherwise dispose of any part of the Leased Property, or any other real property or personal property which may be acquired by the Board, or its interest in the Lease, without the prior written approval of the City.

The City will not sell, transfer or otherwise dispose of real property or personal property included in the Leased Property without the Board's written consent. In the case of personal property, the value of which is less than \$1 million per unit (or of greater value if the Board designates), the Board will adopt rules and procedures for the expedited disposition thereof. Upon the City's request to dispose of any real property or personal property valued in excess of \$1 million, the Board will give such consent only upon receipt of a certificate signed by the Consulting Engineer to the effect that such real or personal property may be disposed of without materially adversely affecting the Revenues of the System or impairing the ability of the Board to make any payments required by the Lease or the Agreement or any other

agreement to which it may be a party or be bound. The City may also, with the prior written consent of the Board, grant interests in the Leased Property which, in the reasonable judgment of the Board, do not interfere with the operation and maintenance of the System and the collection of the Revenues from the System. (*Section 11.1*)

**Encumbrances.** The Board may not encumber the Leased Property without the prior written approval of the City. The City may grant temporary licenses for use of the Leased Property which do not interfere with the operation and maintenance of the System or the collection of Revenues therefrom. (*Section 11.3*)

### **Summary of the Second Resolution**

*Terms used in this Summary of the Second Resolution shall have the meanings ascribed thereto in "APPENDIX C—GLOSSARY AND SUMMARY OF CERTAIN DOCUMENTS—Glossary—Definition of Certain Terms Used in Second Resolution."*

**Pledge of Revenues and Funds.** The Authority pledges for the payment of the Bonds in accordance with their terms and the provisions of the Resolution, subject only to the provisions of the Resolution, the First General Resolution, the Act and the Agreement permitting the application thereof for or to the purposes and on the terms and conditions of the Resolution and therein set forth: (i) all moneys or securities in any of the Funds and Accounts, other than the Arbitrage Rebate Fund, (ii) all Other Moneys, (iii) in moneys or securities on deposit in the FGR Subordinated Indebtedness Fund, except that moneys or securities on deposit in a Special Account are pledged only to the Series of Bonds to which such Account relates and moneys or securities on deposit in the Common Account are pledged only to the Bonds for which a Special Account has not been established pursuant to the Resolution, (iv) all other moneys and securities to be received, held or set aside by the Authority or by any Fiduciary pursuant to the Resolution and (v) from and after the time that the pledge of Revenues made in the First General Resolution shall be discharged and satisfied in accordance with the Resolution, all Revenues; *provided, however,* that such pledge shall be in all respects subordinate to the provisions of the First General Resolution and the lien and pledge created by the First General Resolution. This pledge shall, to the fullest extent permitted by law, be valid and binding from the time when it is made and the Revenues, moneys, securities and other funds so pledged and then or thereafter received by the Authority shall immediately be subject to the lien of such pledge and the obligation to perform the contractual provisions contained in the Resolution and shall be valid and binding as against all parties having claims of any kind in tort contract or otherwise against the Authority, irrespective of whether such parties have notice thereof.

The Act provides that (i) the pledges made by the Resolution are valid, binding and perfected from the time when they are made and property so pledged shall immediately be subject to the lien of such pledges without any physical delivery thereof or further act, (ii) the lien of such pledges shall be valid, binding and perfected as against all parties having claims of any kind in tort, contract or otherwise against the Authority irrespective of whether such parties have notice thereof and (iii) no instrument by which such pledges are created nor any financing statement need be recorded or filed. Accordingly, no financial statements have been or will be filed. Based upon the foregoing, the Authority represents that under the laws of the State (i) the Resolution creates valid and binding pledges in favor of the holders from time to time of the Bonds, enforceable in accordance with the terms set forth in the Resolution, (ii) the pledges made by the Resolution and each pledge made to secure obligations of the Authority which, by the terms set forth in the Resolution, are prior to or of equal rank with such pledge are and shall be prior to any judicial lien hereafter imposed on the property pledged by the Resolution to enforce a judgment against the Authority on a simple contract and (iii) no instrument by which such pledges are created nor any financing statement need be recorded or filed in order to establish or maintain such priority. The Authority further represents that the Authority has not heretofore made a pledge of, granted a lien on or security interest in, or made an assignment or sale of the Revenues or any other property pledged by the Resolution that is prior to or of equal rank with the pledge made by the Resolution and neither the Revenues nor any other property pledged by the Resolution have been described in any financing statement. Except as expressly permitted by the Resolution, the Authority shall not hereafter make or

suffer to exist any pledge or assignment of, lien on or security interest in the Revenues or other property pledged by the Resolution that is prior to or of equal rank with the pledge made by the Resolution, or file any financing statement describing any such pledge, assignment, lien or security interest, except in connection with pledges, assignments, liens or security interests expressly permitted by the Resolution.

As further security for the payment of the principal or Redemption Price of and interest on the Bonds, the Authority assigns, transfers and pledges to the Trustee all of its rights and interests under and pursuant to the Agreement (excluding rights to notice and other procedural rights, its rights to indemnification and rights and interests not material to Bondholders), including, without limiting the generality of the foregoing, the present and continuing right (i) to make claim for, collect or cause to be collected, receive or cause to be received, from the Board all Revenues thereunder, (ii) to bring actions and proceedings thereunder for the enforcement thereof, and (iii) to do any and all things which the Authority is or may become entitled to do under the Agreement; *provided, however* that such assignment, transfer and pledge are and shall be in all respects subject and subordinate to the assignment, transfer and pledge made by the First General Resolution; *provided, further*, that the assignment made by the Resolution shall not impair or diminish any obligation of the Authority under the Agreement.

The Bonds are special obligations of the Authority payable solely from the special funds provided for such payment pursuant to the Act, the First General Resolution and the Resolution and do not and will not constitute an indebtedness of the State, the City or the Board and neither the State, the City nor the Board shall be in any way liable thereon. (*Sections 203 and 501*)

**Establishment of Funds and Accounts.** The Resolution establishes the following Funds:

- (1) Construction Fund;
- (2) Revenue Fund;
- (3) Debt Service Fund;
- (4) Authority Expense Fund;
- (5) Debt Service Reserve Fund;
- (6) Subordinated Indebtedness Fund;
- (7) Arbitrage Rebate Fund; and
- (8) Surplus Fund.

The Resolution establishes in the Debt Service Reserve Fund a separate account known as the “Common Account”, and provides that any Supplemental Resolution which authorizes a (i) Special Credit Facility to secure the payment of the Principal Installments of and interest on the Bonds authorized thereby, (ii) which provides for a Special Credit Facility to secure the payment of the Tender Option Price of any Option Bonds authorized thereby, or (iii) wherein the Authority has determined that the Series of Bonds authorized thereby will not be secured by the Common Account in the Debt Service Reserve Fund, may establish one or more Special Accounts in the Debt Service Reserve Fund. The Resolution also establishes in the Debt Service Fund a separate account to be known as the “Capitalized Interest Account”.

The Trustee shall hold all of the Funds and Accounts.

The Trustee is directed to make withdrawals and transfers from the Funds and Accounts established by the Resolution in order to rebate certain arbitrage earnings to the United States. (*Section 502*)

**Construction Fund.** From and after the date on which no First General Resolution Bonds are Outstanding, the Authority shall deposit from time to time in the Construction Fund the net proceeds from the sale of each Series of Bonds and make the deposits in the Funds and Accounts required by the applicable Supplemental Resolutions. The Authority shall also deposit from time to time in the Construction Fund any other amounts required to be deposited therein pursuant to the Resolution or the Agreement, including amounts received by the Authority for or in connection with the System and

determined by the Authority to be deposited therein. In addition, all moneys on deposit in the Construction Account shall be deposited in the Construction Fund as soon as practicable after the date on which there are no First General Resolution Bonds Outstanding. From and after the date on which no First General Resolution Bonds are Outstanding and proceeds of insurance maintained by the Board or the City against physical loss of or damage to the System, or of contractors' performance bonds pertaining to the construction of the System, shall also be paid into the Construction Fund.

Except as otherwise provided, amounts in the Construction Fund, and subject to the provisions of the First General Resolution, the Construction Account may only be expended to pay Costs of Water Projects (including Costs of Issuance). The Trustee shall, subject to certain exceptions contained in the First General Resolution and the Resolution, make payments from the Construction Fund, except as otherwise provided, only upon receipt of a Disbursement Request signed by an Authorized Representative of the Authority.

To the extent that other moneys are not available therefor in any other Fund or Account, amounts in the Construction Fund and Construction Account shall be applied to the payment of principal of and interest on Bonds and of the interest on Parity Bond Anticipation Notes when due. The Authority will cause moneys in the Construction Account to be transferred to the Debt Service Fund at such time and in such amount as may be required for such purpose. (*Section 504*)

**Allocation of Revenues—Revenue Fund.** The Authority shall cause all Other Moneys and, from and after the date on which no First General Resolution Bonds are Outstanding, all Revenues received from the Board pursuant to the Agreement to be paid to the Trustee and deposited promptly upon receipt in the Revenue Fund. There shall also be deposited in the Revenue Fund all other amounts required by the Resolution or the Agreement to be so deposited.

In addition to the payments to be made from the Subordinated Indebtedness Fund, as soon as practicable in each month the amount in the Subordinated Indebtedness Fund (other than in the Construction Account) shall be transferred to the Revenue Fund until the amount on deposit therein is equal to the sum of:

(i) together with the amount in the Debt Service Fund, the Monthly Balance for such month and the amount necessary to pay the purchase price or Redemption Price of Bonds purchased or called for redemption; plus

(ii) the amount, if any, necessary to make the total on deposit in the Debt Service Reserve Fund and credited to the Common Account equal to the Debt Service Reserve Requirement for the Bonds to which such Common Account relates, and to make the total on deposit in each Special Account equal to the Debt Service Reserve Requirement for the Bonds to which each such Special Account relates; plus

(iii) the amount, if any, then required to be in the Subordinated Indebtedness Fund. (*Section 505*)

**Payments Into Certain Funds.** From the Revenues in the Revenue Fund, the Trustee shall make, as soon practicable in each month, the following deposits in the following order:

(i) to the Debt Service Fund, all such amounts until the total on deposit therein equals the sum of (A) the Monthly Balance for such month for all Series of Bonds Outstanding and (B) the amount necessary to pay the purchase price or Redemption Price of Bonds purchased or called for redemption;

(ii) if no First General Resolution Bonds are then Outstanding, from the balance, if any, remaining in such month after making the deposits required by paragraph (i) to the Authority Expense Fund the entire balance until the total on deposit therein in such month is equal to the product obtained by multiplying (A) the sum of (i) the Authority Expenses for the then current Fiscal Year as set forth in the Authority Budget, plus (ii) if included in the Authority Budget for the then current Fiscal Year, an amount (“the Reserve for Expenses”) equal to one-sixth of such Authority Expenses by (B) a fraction, the numerator of which is twelve (12) minus the number of full months (excluding the month of calculation) remaining in the Fiscal Year and the denominator of which is twelve (12);



(iii) from the balance, if any remaining after making the deposits required by paragraphs (i) and (ii), to the Debt Service Reserve Fund, first, to the credit of the Common Account therein the amount, if any, necessary to make the total on deposit in such Fund and credited to the Common Account equal to the Debt Service Reserve Requirement for the Bonds to which such Common Account relates, or, the entire balance if less than sufficient and, then, from the balance of such deposit, if any, remaining after crediting the Common Account as aforesaid, to the credit of each Special Account an amount equal to the Debt Service Reserve Requirement for the Bonds to which each such Special Account relates; *provided, however*, that if the balance remaining is less than sufficient to credit in full each Special Account, credit shall be made pro rata among all Special Accounts in the same ratio as the Debt Service Reserve Requirement related to each Special Account bears to the sum of the Debt Service Reserve Requirements for all the Bonds related to Special Accounts:

(iv) from the balance, if any, remaining after making the deposits required by paragraphs (i), (ii) and (iii) to the Arbitrage Rebate Fund, the amount, if any, equal to the earnings in investments in the Debt Service Reserve Fund which were transferred to the Revenue Fund in the preceding month; and

(v) from the balance, if any, remaining after making the deposits required by paragraphs (i), (ii), (iii) and (iv) and if no First General Resolution Bonds are then Outstanding, to the Subordinated Indebtedness Fund the amount required to be deposited in such Fund for such month in accordance with the Authority Budget to the entire balance if less than sufficient.

Beginning with the first day of each Fiscal Year, the Authority shall cause to be calculated the amounts deposited in the Revenue Fund on a daily basis until it is determined that the total of all amounts deposited therein during such Fiscal Year is at least equal to the SGR Cash Flow Requirement. Thereafter, during such Fiscal Year, no further amounts on deposit in the FGR Subordinated Indebtedness Fund shall be required to be deposited in the Revenue Fund; *provided, however*, if the Authority shall thereafter certify an amended Authority Budget for such Fiscal Year showing an SGR Cash Flow Requirement in excess of the SGR Cash Flow Requirement last certified for such Fiscal Year, calculation of the amounts deposited in the Revenue Fund on a daily basis shall be resumed until it is determined that the total of all amounts deposited therein during such Fiscal Year is at least equal to the SGR Cash Flow Requirement, as amended. Thereafter, during such Fiscal Year, no further amounts on deposit in the FGR Subordinated Indebtedness Fund shall be required to be deposited in the Revenue Fund, unless the Authority thereafter, in such Fiscal Year, again certifies an amended Authority Budget showing an SGR Cash Flow Requirement in excess of the SGR Cash Flow Requirement theretofore certified in such Fiscal Year. (*Section 506*)

**Debt Service Fund.** The Trustee shall for the Outstanding Bonds of a Series, Parity Bond Anticipation Notes and Parity Reimbursement Obligations, pay (i) on each Bond Payment Date, (1) from the moneys on deposit in the Debt Service Fund the amounts required for the payment of the Principal Installments, if any, due on such Bond Payment Date and (2) from the moneys on deposit in the Debt Service Fund, including the moneys credited to the subaccount, if any, established for such Series in the Capitalized Interest Account in such Fund, the interest due on such Bond Payment Date, (ii) on any redemption date or date of purchase, the amounts required for the payment of accrued interest on Bonds to be redeemed or purchased on such date unless the payment of such accrued interest shall be otherwise provided and (iii) on each Bond Payment Date for Parity Bond Anticipation Notes, the interest due thereon on such Bond Payment Date, including from moneys credited to the sub-account, if any, established for such Parity Bond Anticipation Notes in the Capitalized Interest.

The Trustee may, and if so directed by an Authorized Representative of the Authority shall, prior to the forty-fifth day preceding the due date of each Sinking Fund Installment, apply the amounts accumulated in the Debt Service Fund for such Sinking Fund Installment, together with any interest on the Bonds for which such Sinking Fund Installment was established: (i) to the purchase of Bonds of like Series and maturity at prices (including any brokerage and other charges) not exceeding the Redemption Price payable for such Bonds when such Bonds are redeemable with such Sinking Fund Installment plus

unpaid interest accrued or (ii) to the redemption of such Bonds, if redeemable by their terms, at or below said Redemption Price. Upon such purchase or redemption of any Bond, the Trustee shall then credit an amount equal to the principal of the Bond so purchased or redeemed toward the next Sinking Fund Installments thereafter to become due and the amount of any excess over the amount of such Sinking Fund Installment shall be credited against future Sinking Fund Installments in direct chronological order.

In any event, the Trustee shall, as soon as practicable after the forty-fifth day preceding the due date of any such Sinking Fund Installment, call for redemption a sufficient amount of Bonds of like Series and maturity to complete the retirement of the principal amount specified for such Sinking Fund Installment of such Bonds whether or not it then has moneys in the Debt Service Fund to pay the applicable Redemption Price thereof on redemption date. The Trustee shall apply to the redemption of the Bonds on each such redemption date the amount required for the redemption of such Bonds.

In the event of the refunding of any Bonds, the Trustee shall, upon the written direction of the Authority, withdraw from the Debt Service Fund and the Capitalized Interest Account related to the Bonds to be refunded all or any portion of amounts accumulated therein with respect to the Bonds to be refunded and deposit such amounts as provided in such written direction; *provided, however*, that such withdrawal shall not be made unless (i) immediately thereafter the Bonds being refunded shall be deemed to have been paid, and (ii) after giving effect to any amounts being simultaneously deposited therein the amount remaining in the Debt Service Fund after such withdrawal shall not be less than the Monthly Balance at the date of such withdrawal with respect to Bonds then Outstanding, after the Bonds to be refunded have been deemed paid. (*Section 507*)

**Authority Expense Fund.** The Authority shall apply amounts credited to the Authority Expense Fund to the payment of Authority Expenses. Any moneys in the Authority Expense Fund which the Authority determines are in excess of that needed to meet the sum of the unpaid Authority Expenses for such Fiscal Year plus (if such amount was included in the Authority Budget for such Fiscal Year) the Reserve for Expenses shall be applied toward any deficiencies in the following Funds and Accounts in the order stated: the Debt Service Fund, Debt Service Reserve Fund and Subordinated Indebtedness Fund. Any remaining amounts shall be credited to the Revenue Fund. (*Section 508*)

**Debt Service Reserve Fund.** The Resolution establishes a Debt Service Reserve Fund and a Common Account therein. In addition, the Resolution provides that any Supplemental Resolution which provides (i) for a Special Credit Facility to secure the payment of the Principal Installments of and interest on the Bonds authorized thereby, (ii) which provides for a Special Credit Facility to secure the payment of the Tender Option Price of any option Bonds authorized thereby, or (iii) wherein the Authority has determined that the Series of Bonds authorized thereby will not be secured by the Common Account in the Debt Service Reserve Fund, may establish one or more Special Accounts in the Debt Service Reserve Fund. From the proceeds of each Series of Bonds there shall be deposited in the Debt Service Reserve Fund the amount, if any, necessary to make the amount on deposit therein equal to the Debt Service Reserve Requirement, after giving effect to the issuance of such Bonds; and all such amounts will be credited to the Common Account, unless a Supplemental Resolution requires a deposit in a Special Account.

Amounts on deposit in the Common Account will be applied, to the extent necessary, to pay the Principal Installments of and interest on the Bonds; *provided, however*, that the amounts in the Common Account may not be applied to pay the Principal Installments of and interest on, or Tender Option Price of or interest on, Bonds for which such payments are secured by a Special Credit Facility, or to pay Principal Installments of and interest on Bonds that the Authority has determined will not be secured by amounts in the Common Account; these Bonds will be secured by amounts, if any, on deposit in the Special Account. Likewise, amounts in any Special Account may not be applied to pay the Principal Installments of or interest on any Bond for which such payments may be made from the Common Account. Amounts on deposit in each of the Accounts in the Debt Service Reserve Fund shall be applied, to the extent other funds are not available pursuant to the Resolution to pay the Principal Installments of, and interest on the Bonds to which such Account relates when due. Amounts so applied shall be derived first from cash or Investment Securities on deposit, and then from draws and demands on

Financial Guaranties; *provided, however*, that if more than one Financial Guaranty is held in an Account at the time moneys are to be withdrawn therefrom the Trustee shall obtain payment under each such Financial Guaranty pro rata based upon the respective amounts then available to be paid thereunder.

If, as of June 30 of each year, the amount in any Account in the Debt Service Reserve Fund exceeds the applicable Debt Service Reserve Requirement after giving effect to any Financial Guaranty deposited in such Fund, the Trustee shall, on the first business day of the following Fiscal Year, withdraw from such Account the amount of any excess therein over the applicable Debt Service Reserve Requirement as of the date of such withdrawal for deposit into (i) the Arbitrage Rebate Fund, the amount estimated by the Authority to be required by the Code to be rebated to the Department of the Treasury, and (ii) the Reserve Fund, the amount of any excess then remaining in the Debt Service Reserve Fund over the applicable Debt Service Reserve Fund Requirement. If, as of February 1 of each year the amount in any Account in the Debt Service Reserve Fund is less than the applicable Debt Service Reserve Requirement and, to the extent that such deficiency has not been made up by May 1 of such year by either (i) deposits pursuant to Sections 506, 511 or 512 of the Resolution or (ii) an increase in the market value of the securities therein or (iii) a combination of (i) and (ii), the Authority shall, in its Authority Budget for the ensuing Fiscal Year, include the amount necessary to make up such deficiency as a Required Deposit.

Whenever the amount (exclusive of Financial Guaranties) in all of the Accounts in the Debt Service Reserve Fund, together with the amount in the Debt Service Fund, is sufficient to pay all Outstanding Bonds in accordance with their respective terms, the funds on deposit in the Debt Service Reserve Fund shall be transferred to the Debt Service Fund and applied to the redemption or payment at maturity of all Bonds Outstanding.

In lieu of or in substitution for moneys or Investment Securities otherwise required to be deposited in the Common Account of the Debt Service Reserve Fund, the Authority may deposit or cause to be deposited with the Trustee a Financial Guaranty for the benefit of the Holders of the Bonds for all or any part of the Debt Service Reserve Requirement; *provided, however*, (i) that any such surety bond or insurance policy shall be issued by an insurance company or association duly authorized to do business in the State and either (A) the claims paying ability of which is rated the highest rating accorded by a nationally recognized rating agency, or (B) obligations insured by a surety bond or an insurance policy issued by such company or association and rated at the time such surety bond or insurance policy is delivered, without regard to qualification of such rating by symbols such as “+” or “-” or numerical notation, in the highest rating category by each Rating Agency or, if Outstanding Bonds are not rated by both Rating Agencies, by whichever Rating Agency that then rates Outstanding Bonds and (ii) that any such letter of credit shall be issued by a bank, a trust company, a national banking association, a corporation subject to registration with the Board of Governors of the Federal Reserve System under the Bank Holding Company Act of 1956 or any successor or provision of law, a federal branch pursuant to the International Banking Act of 1978 or any successor provision of law or a domestic branch or agency of a foreign bank which branch or agency is duly licensed or authorized to do business under the laws of any state or territory of the United States of America, the unsecured or uncollateralized long term debt obligations of which, or long term obligations secured or supported by a letter of credit issued by such person, are rated at the time such letter of credit is delivered, without regard to qualification of such rating by symbols such as “+”, or “-” or numerical notation, in at least the second highest rating category by each Rating Agency or, if Outstanding Bonds are not rated by both Rating Agencies, by whichever Rating Agency that then rates Outstanding Bonds.

In addition to the conditions and requirements set forth above, no Financial Guaranty shall be deposited in full or partial satisfaction of the Debt Service Reserve Requirement unless the Trustee shall have received prior to such deposit (i) an opinion of counsel to the effect that such Financial Guaranty has been duly authorized, executed and delivered by the Financial Guaranty Provider thereof and is valid, binding and enforceable in accordance with its terms, (ii) in the event such Financial Guaranty Provider is not a domestic entity, an opinion of foreign counsel in form and substance satisfactory to the Trustee and (iii) in the event such Financial Guaranty is a letter of credit, an opinion of counsel acceptable to the Trustee and to each Financial Guaranty Provider substantially to the effect that payments under such

letter of credit will not constitute avoidable preferences under Section 547 of the United States Bankruptcy Code in a case commenced by or against the Authority thereunder or under any applicable provisions of the Debtor and Creditor Law of the State.

Notwithstanding the foregoing, if at any time after a Financial Guaranty has been deposited with the Trustee the ratings on any Outstanding Bonds are less than in the second highest rating category by each Rating Agency, without regard to qualification of such rating by symbols such as “+” or “-” or numerical notation, and the unsecured or uncollateralized long term debt of the Financial Guaranty Provider or the long term debt obligations secured or supported by a surety bond, insurance policy or letter of credit of a Financial Guaranty Provider is reduced below the third highest rating category by each Rating Agency, without regard to qualification of such rating by symbols such as “+” or “-” or numerical notation, the Authority shall either (i) replace or cause to be replaced said Financial Guaranty with another Financial Guaranty which satisfies the requirements of the two preceding paragraphs or (ii) deposit or cause to be deposited in the Debt Service Reserve Fund an amount of moneys equal to the value of the Financial Guaranty of such Financial Guaranty Provider, such deposits to be, as nearly as practicable, in ten equal semi-annual installments commencing on the earlier of the December 15 or June 15 next succeeding the reduction in said ratings.

Each Financial Guaranty shall be payable (upon the giving of such notice as may be required thereby) on any date on which moneys are required to be withdrawn from the Debt Service Reserve Fund and such withdrawal cannot be made without drawing upon such letter of credit or obtaining payment under such surety bond or insurance policy.

For the purposes of the above provisions under the heading “Debt Service Reserve Fund”, and the provisions under the heading “Investment of Certain Funds” below, in computing the amount on deposit in the Debt Service Reserve Fund, a letter of credit, a surety bond or an insurance policy shall be valued at the amount available to be drawn or payable thereunder on the date of computation: *provided, however*, that, if the unsecured or uncollateralized long term debt of the Financial Guaranty Provider thereof, or the long term debt obligations secured or supported by a surety bond, insurance policy or letter of credit of said Financial Guaranty Provider has been reduced below the ratings required by the third paragraph under the heading “Debt Service Reserve Fund”, said Financial Guaranty shall be valued at the lesser of (i) the amount available to be paid thereunder on the date of calculation and (ii) the difference between the amount available to be paid thereunder on the date of issue thereof and an amount equal to a fraction of such available amount the numerator of which is the aggregate number of December 15th’s and June 15th’s which has elapsed since such ratings were reduced and the denominator of which is ten.

With respect to any demand for payment under any Financial Guaranty, the Trustee shall make such demand for payment in accordance with the terms of such Financial Guaranty in a timely manner to assure the availability of moneys on the Bond Payment Date for which such moneys are required.

In the event of the refunding of any Bonds, the Trustee shall, upon the written direction of the Authority, withdraw from the Debt Service Reserve Fund all or any portion of amounts accumulated therein with respect to the Bonds being refunded and deposit such amounts as provided in such written direction; provided that such withdrawal shall not be made unless (a) immediately thereafter the Bonds being refunded shall be deemed to have been paid pursuant to Section 1201 of the Resolution, and (b) the amount remaining in the Debt Service Reserve Fund after such withdrawal shall not be less than the Debt Service Reserve Requirement. (*Section 509*)

**Subordinated Indebtedness Fund.** The Trustee shall apply amounts on deposit in the Subordinated Indebtedness Fund solely to the maintenance of reserves for, or the payment of, Subordinated Indebtedness (or as otherwise provided by the resolution of the Authority authorizing each issue of Subordinated Indebtedness). The Trustee shall withdraw from the Subordinated Indebtedness Fund any amount necessary to render the balances in the Debt Service Fund or Debt Service Reserve Fund sufficient to meet the requirements of such Funds. (*Section 510*)

**Arbitrage Rebate Fund.** Amounts on deposit in the Arbitrage Rebate Fund shall be applied by the Trustee to make payments to the Department of the Treasury of the United States of America.

Notwithstanding the foregoing, the Trustee shall apply moneys credited to the Arbitrage Rebate Fund in the following amounts: (i) to the Debt Service Fund the amount, if any, necessary (or all the moneys in the Arbitrage Rebate Fund if less than the amount necessary) to make up any deficiency in the amount required to be on deposit in the Debt Service Fund and (ii) to the Debt Service Reserve Fund the amount, if any, necessary (or all the moneys in the Arbitrage Rebate Fund if less than the amount necessary) to make up any deficiency in the amount required to be on deposit in any Account in the Debt Service Reserve Fund.

Amounts on deposit in the Arbitrage Rebate Fund in excess of the amount required to be maintained therein or the purposes of such Fund may be transferred and paid by the Trustee to the Revenue Fund. *(Section 511)*

**Surplus Fund.** The Trustee shall, on each Bond Payment Date, apply moneys credited to the Surplus Fund in the following amounts: (i) to the Debt Service Fund the amount, if any, necessary (or all the moneys in the Surplus Fund if less than the amount necessary) to make up any deficiency in the amount required to be on deposit in such Fund and (ii) to the Debt Service Reserve Fund the amount, if any, necessary (or all the moneys in the Surplus Fund if less than the amount necessary) to make up any deficiency in the amount required to be on deposit in any Account in such Fund. Such transfer shall be made notwithstanding any other provisions of the Resolution requiring deposits in such Funds. Amounts on deposit in the Surplus Fund on the last day of a Fiscal Year shall be withdrawn from such Fund and transferred to the Board for deposit in the Local Water Fund. *(Section 512)*

**Depositaries.** All moneys or securities held by the Trustee under the provisions of the Resolution shall constitute trust funds and the Trustee may, and shall, if directed in writing by an Authorized Representative of the Authority deposit such moneys or securities with one or more Depositaries in trust for the Trustee. All moneys or securities deposited under the provisions of the Resolution with the Trustee or any Depository shall be held in trust and applied only in accordance with the provisions of the Resolution and the applicable provisions of the First General Resolution, and each of the Funds and the Accounts shall be a trust fund for the purposes thereof. The Authority and the Trustee shall instruct each Depository that any moneys or securities credited to a Fund or an Account under the Resolution which are deposited with such Depository shall be identified to be part of such Fund or Account and subject to the pledge in favor of the Trustee created under the Resolution. Prior to the first deposit of any moneys or securities with each Depository, the Authority and the Trustee shall obtain from such Depository its agreement to serve as agent of the Trustee in holding such moneys or securities in pledge in favor of the Trustee and the contract or other written instrument between the Authority and such Depository governing the establishment and operation of such account shall provide the moneys or securities from time to time deposited with such Depository shall be held by such Depository as such agent in pledge in favor of the Trustee; *provided, however*, that, except as otherwise expressly provided in the Resolution, the Authority shall be permitted at any time to make withdrawals from and write checks or other drafts against any account held by the Authority and established with such Depository and apply the same for the purposes specified in the Resolution and, subject to Section 515 of the Resolution, the Authority shall be permitted to invest amounts in any such account in Investment Securities.

Each Depository holding moneys or securities in trust for the Trustee shall be a bank or trust company organized under the laws of the State or a national banking association (having its principal office within the State), having capital stock, surplus and undivided earnings aggregating at least \$100,000,000 (or such greater amount as set forth in a Supplemental Resolution) and willing and able to accept the office on reasonable and customary terms and authorized by law to act in accordance with the provisions of the Resolution. *(Section 513)*

**Investment of Certain Funds.** Moneys held in the Debt Service Fund, the Debt Service Reserve Fund and the Subordinated Indebtedness Fund (subject to the terms of any resolutions or other instrument securing any issue of Subordinated Indebtedness) shall be invested and reinvested to the fullest practical extent in Investment Securities which mature not later than such times as shall be necessary to provide moneys when needed to make payments required from such Funds; provided that in the case of the Debt Service Fund, investments shall be of the type described in clauses (ii), (iii) or

(iv) of the definition of "Investment Securities." Moneys in the Authority Expense Fund, the Revenue Fund, the Construction Fund, the Arbitrage Rebate Fund and the Surplus Fund may be invested and reinvested in Investment Securities which mature later than such times as shall be necessary to provide moneys when needed to make payments from such Funds. The Trustee shall make all investments in accordance with the direction of an Authorized Representative of the Authority, given either in writing, which may be sent by electronic transmission of a facsimile, or by telephonic communication subsequently confirmed in writing. Moneys in any Fund or Account may be combined with moneys in any other Fund or Account for the purpose of making such investments in Investment Securities.

Interest (net of that which represents a return of accrued interest paid in connection with the purchase of any investment) and other investment earnings on any moneys or investments in the Funds and Accounts, other than the Construction Fund, the Debt Service Reserve Fund and the Arbitrage Rebate Fund, shall be paid into the Revenue Fund as and when received. Interest (net of that which represents a return of accrued interest paid connection with the purchase of any investment) and other investment earnings on any moneys or investments in (i) the Debt Service Reserve Fund shall be paid into the Arbitrage Rebate Fund, the Surplus Fund or the Revenue Fund; (ii) the Arbitrage Rebate Fund shall remain in such Fund; and (iii) the Construction Fund shall be paid quarterly, on the fifteenth day of each July, October, January and April of each Fiscal Year, to the Board deposit in the Local Water Fund; *provided, however*, that no such payment shall be made unless the Trustee shall receive (A) the written direction of an Authorized Representative of the Authority to make such payment and (B) a Certificate of an Authorized Representative of the Authority stating that, as of the date thereof, there has been deposited in the Revenue Fund during such Fiscal Year an amount equal to the Cash Flow Requirement.

All Investment Securities acquired with moneys in any Fund or Account shall be held by the Trustee in pledge or by a Depository as agent in pledge in favor of the Trustee. (*Section 515*)

**Additional Bonds.** In order to provide sufficient funds for the Costs of Water Projects or for the purpose refunding any Bonds, First General Resolution Bonds or any other bonds, notes or other obligations issued either by the Authority or the City to pay the capital costs of the System, Bonds of the Authority are authorized to be issued from time to time without limitations as to amount except as provided in the Resolution or as may be limited by law and such Bonds shall be issued subject to the terms, conditions and limitations established in the Resolution and in one or more Series as therein provided.

Bonds shall be authenticated and delivered only upon the Trustee's receipt of, among other items:

(a) a Bond Counsel's Opinion as to validity and certain other matters required by the Resolution;

(b) a certified copy of the Supplemental Resolution authorizing such Series;

(c) an executed copy of an amendment or supplement to the Agreement or the Lease not theretofore delivered to the Trustee;

(d) except in the case of any Series of Refunding Bonds issued pursuant to Section 207 of the Resolution, a Certificate of an Authorized Representative of the Authority setting forth (i) the Revenues for either of the last two full Fiscal Years immediately preceding the Fiscal Year in which such bonds are to be issued and (ii) the Aggregate Debt Service on First General Resolution Bonds, Outstanding Bonds, Parity Bond Anticipation Notes and Parity Reimbursement Obligations during such Fiscal Year for which Revenues are set forth pursuant to clause (i), excluding from Aggregate Debt Service the amount thereof which was paid from sources other than Revenues, and (iii) the sum of the Operating Expenses and the Required Deposits for such Fiscal Year (exclusive of Required Deposits for the payment of Outstanding Bonds, Parity Bond Anticipation Notes and Parity Reimbursement Obligations), and showing that the amount set forth in (i) is at least equal to the sum of (x) 110% of the amount set forth in (ii) and (y) 100% of the amount set forth in (iii);

(e) except in the case of Refunding Bonds issued pursuant to Section 207 of the Resolution, a Certificate of each of the respective Authorized Representatives of the Authority, the Board and

City, each dated as of the date of such delivery, stating that (i) the Authority is not in default in the performance of any of the covenants, conditions, agreements or provisions contained in the Resolution, (ii) the Board is not in default in the performance of any of the covenants, conditions, agreements or provisions contained in the Agreement or the Lease and (iii) the City is not in default in the performance of any of the covenants, conditions, agreements or provisions contained in the Agreement or the Lease;

(f) a Certificate signed by an Authorized Representative of the Authority setting forth the Cash Flow Requirement as of such date; and

(g) in the case of any Series for which Capitalized Interest has been provided by the Supplemental Resolution authorizing such Series, (i) the written direction of an Authorized Representative of the Authority to establish the sub-account for such Series in the Capitalized Interest Account in the Debt Service Fund and (ii) the amount of the proceeds of such Series to be deposited in the Subordinated Indebtedness Fund for payment to such sub-account. (*Sections 204 and 206*)

**Refunding Bonds.** One or more Series of Refunding Bonds may be issued pursuant to Section 207 of the Resolution at any time to refund any Outstanding Bonds only upon the Trustee's receipt of, among other things, a Certificate signed by an Authorized Representative of the Authority stating that (a) the average annual Debt Service on the Refunding Bonds of such Series does not exceed the average annual Debt Service on the Bonds to be refunded and (b) the maximum Debt Service in any Fiscal Year on the Refunding Bonds of such Series shall not exceed the maximum Debt Service in any Fiscal Year on the Bonds to be refunded. (*Section 207*)

**Bond Anticipation Notes.** The Authority may, by resolution, authorize the issuance of notes (and renewals thereof in anticipation of the issuance of a Series of Bonds. The principal of and interest on such notes and renewals thereof shall be payable from the proceeds of such notes or from the proceeds of the sale of the Series of Bonds issued to provide for the payment of such notes. The proceeds of such Bonds may be pledged for the payment of the principal of and interest on such notes and any such pledge shall have a priority over any other pledge of such proceeds created by the Resolution. The Authority may also pledge (i) the Funds and Accounts, other than the Arbitrage Rebate Fund, and (ii) the Revenues to the payment of the interest on, and subject to Section 706 of the Resolution, the principal of such notes. A copy of the Resolution of the Authority authorizing such notes, certified by an Authorized Representative of the Authority, shall be delivered to the Trustee following its adoption, together with such other information concerning such notes as the Trustee may reasonably request. (*Section 208*)

**Credit Facilities and Interest Rate Exchange Agreements.** In connection with the issuance of any Series of Bonds or Parity Bond Anticipation Notes, the Authority may obtain or cause to be obtained one or more Credit Facilities providing for payment of all or a portion of the Principal Installments, Redemption Price or interest due or to become due on such Bonds or the principal or interest due or to become due on such Parity Bond Anticipation Notes, providing for the purchase of such Bonds by the issuer of such Credit Facility or Revolving funds for the purchase of such Bonds by the Authority. In connection therewith the Authority may enter into such agreements with the issuer of such Credit Facility providing for, among other things: (i) reimbursement of the issuer of the Credit Facility for amounts paid under the terms thereof; *provided, however*, that no obligation to reimburse such issuer shall be created, for purposes of the Resolution, until amounts are paid under such Credit Facility; (ii) the payment of fees and expenses to such issuer for the issuance of such Credit Facility; (iii) the terms and conditions of such Credit Facility and the Series of Bonds or the Parity Bond Anticipation Notes affected thereby; and (iv) the security, if any, to be provided for the issuance of such Credit Facility'. The Authority may secure such Credit Facility by an agreement providing for the purchase of the Series of Bonds secured thereby with such adjustments to the rate of interest, method of determining interest, maturity, or redemption provisions as specified by the Authority in the applicable Supplemental Resolution. Any such Credit Facility shall be for the benefit of and secure such Series of Bonds or portion thereof as specified in the applicable Supplemental Resolution.

In connection with the Bonds of any Series or Parity Bond Anticipation Notes, the Authority may enter into one or more Interest Rate Exchange Agreements providing for, inter alia: (i) the payment of fees, expenses and other amounts to the Counterparty; (ii) the terms and conditions of such Interest Rate Exchange Agreements; (iii) the Bonds of the Series or Parity Bond Anticipation Notes to which such Interest Rate Exchange Agreement relate; and (iv) the security, if any, to be provided by the Authority or the Counterparty for performance of their respective obligations under the Interest Rate Exchange Agreement.

The Authority may also in an agreement with the issuer of a Credit Facility agree to reimburse such issuer directly for amounts paid under the terms of such Credit Facility, together with accrued interest thereon; *provided, however*, that no obligation to reimburse an issuer of a Credit Facility shall be created, for purposes of the Resolution, until amounts are paid under such Credit Facility. Such payments to reimburse the issuer of a Credit Facility and the obligations of the Authority to make payments to a Counterparty, are referred to in the Resolution as a “Reimbursement Obligation.” Any Reimbursement Obligation (a “Parity Reimbursement Obligation”) may be secured by a pledge of and a lien on, the Revenues, Other Moneys, the Funds and Accounts (other than the Arbitrage Rebate Fund) and amounts in the FGR Subordinated Indebtedness Fund on a parity with the lien created thereon by Section 501 of the Resolution; *provided, however*, that with respect to Parity Bond Anticipation Notes, such pledge and lien may secure only the Authority’s Reimbursement Obligation incurred on account of amounts advanced for the payment of the interest on such Parity Bond Anticipation Notes unless the principal amount of such Reimbursement Obligation which was advanced on account of the principal of such Parity Bond Anticipation Notes is payable to the provider of the Credit Facility in substantially equal installments payable over not less than eight calendar quarters. Any such Parity Reimbursement Obligation shall be deemed to be a part of the Series or Parity Bond Anticipation Notes to which the Credit Facility or Interest Rate Exchange Agreement, as the case may be, which gave rise to such Parity Reimbursement Obligation relates. (*Section 209*)

**Indebtedness and Liens.** The Resolution provides that the Authority shall not issue any bonds, notes, or other evidences of indebtedness or otherwise incur any indebtedness, other than the First General Resolution Bonds, Bonds, Parity Bond Anticipation Notes or Parity Reimbursement Obligations, secured by a pledge of or other lien or charge on the Revenues or any of the assets pledged which is prior to or of equal rank or priority with the pledge made and shall not create or cause to be created any lien or charge on the Revenues or on any of the assets pledged which is prior to or of equal rank or priority with the pledge made; *provided, however*, that, with respect to Bond Anticipation Notes, such lien or pledge shall secure payment of the interest thereon, unless the principal thereof shall be secured by a lien on the Revenues as hereinafter provided in this paragraph. This paragraph shall not prevent the Authority from issuing bonds, other notes or other obligations for the corporate purposes of the Authority payable out of, or secured by a pledge of, Revenues to be derived on and after such date as the pledge of the Revenues provided in the Resolution shall be discharged and satisfied as provided in Section 1201 of the Resolution, or from issuing bonds or notes or other obligations for the corporate purposes of the Authority which are payable out of or secured by the pledge of amounts available therefor in the Local Water Fund after satisfaction, in each Fiscal Year, of the Cash Flow Requirement for such Fiscal Year and which recite on their face that such pledge of said amounts is and shall be in all respects subordinate to the provisions of the Resolution and the lien and pledge created by the Resolution.

The Authority will not issue any bonds, notes or other evidences of indebtedness or otherwise incur any indebtedness, other than Bonds or First General Resolution Bonds, payable from, or secured by a pledge of or other lien or charge on the Construction Account of the FGR Subordinated Indebtedness Fund. (*Section 706*)

**Agreement of the State.** In accordance with Section 1045-t of the Act, the Authority agrees, for and on behalf of the State, that the State will not alter or limit the rights vested by the Act in the Authority or the Board to shall the terms of any agreement made with or for the benefit of the Bondholders, or in any way impair the right, and remedies of Bondholders, until the Bonds, together with the interest thereon, with interest on any unpaid installment of interest, and all costs and expenses in connection with any action or proceeding by or on behalf of such holders, are fully met and discharged. (*Section 709*)



**Authority Budget.** The Authority shall, on or before May 1, in each Fiscal Year, adopt and file with the Trustee, the Board and the City, a copy of the Authority Budget, duly certified by an Authorized Representative of the Authority, showing the estimated Cash Flow Requirement (including the amount of each item constituting a component thereof, on a monthly basis) for the ensuing Fiscal Year, together with the estimated Revenues, other than Revenues to be received from the Board pursuant to the Agreement, expected to be received by the Authority in the ensuing Fiscal Year, and any other information required to be set forth therein by the Resolution or the Agreement. Such Authority Budget may set forth such additional information as the Authority may determine or as the Board or the City may request.

If for any reason the Authority shall not have adopted the Authority Budget before May 1, the Authority Budget for the then current Fiscal Year shall be deemed to be the Authority Budget for the ensuing Fiscal Year until new Authority Budget is adopted.

The Authority may at any time adopt an amended Authority Budget for the then current or ensuing Fiscal Year, but no such amended Authority Budget shall supersede any prior Budget until the Authority shall have filed with the Trustee, the Board and the City a copy of such amended Authority Budget. *(Section 710)*

**Cash Flow Requirement.** On the first day of each month after the adoption of the Authority Budget for any Fiscal Year, the Authority shall recalculate the Cash Flow Requirement for such Fiscal Year. If any such recalculation results in the determination of a Cash Flow Requirement in excess of the Cash Flow Requirement set forth in the then current Authority Budget, the Authority shall adopt and file an amended Authority Budget in accordance with Section 711(c) of the Resolution.

At any time on or after May 1 of a Fiscal Year, but not later than June 15 of such Fiscal Year, the Authority shall recalculate the Cash Flow Requirement for such Fiscal Year and include therein, in addition to all other amounts required by the Resolution or by the Agreement or First General Resolution to be included therein, an amount equal to the lesser of (i) the amount estimated to be in the Local Water Fund on June 30 of such Fiscal Year after the Board has made the payments and deposits required by paragraphs FIRST through SEVENTH of Section 4.2(c) of the Agreement and (ii) an amount equal to the difference between (x) the Aggregate Debt Service on Bonds, Parity Bond Anticipation Notes and Parity Reimbursement Obligations payable during the next succeeding Fiscal Year, less (y) the Other Moneys projected to be received during such next succeeding Fiscal Year. Upon such recalculation the Authority shall adopt and file an amended Authority Budget in accordance with Section 711(c) of the Resolution.

If a Financial Guaranty is to expire or terminate during a Fiscal Year and as a result thereof the amount in the Debt Service Reserve Fund would be less than the Debt Service Reserve Requirement, the Authority shall include in the Authority Budget and the Cash Flow Requirement for such Fiscal Year and for each of the four Fiscal Years next succeeding such Fiscal Year an amount equal to twenty percent (20%) of the deficit in the Debt Service Reserve Fund created by such expiration or termination, unless prior to adoption of the Authority Budget for any such Fiscal Year the Authority has obtained an extension of or substitute for such Financial Guaranty or a commitment for the issuance of such extension or substitute. *(Section 711)*

**Enforcement and Amendment of Agreement and Lease.** The Authority shall enforce or cause to be enforced the provisions of the Agreement and the Lease and duly perform its covenants and agreements under the Agreement. The Authority will not consent or agree to or permit any rescission of or amendment to or otherwise take any action under or in connection with the Agreement or the Lease except in accordance with Article X or the Agreement and Section 714 of the Resolution. *(Section 713)*

**Amendments to First General Resolution, Agreement and Lease.** Except as otherwise provided in the Resolution, the First General Resolution, the Agreement or the Lease may not be amended, changed, modified or terminated, nor may any provision thereof be waived, without the consent of the Holders of Outstanding Bonds as provided in the Resolution, if such amendment, change, modification, termination or waiver:

(i) amends subsection (c)(ii), (c)(iii), (g), (h), (i), (j), (k) or (l) of Section 206 of the First General Resolution:

(ii) amends Section 207 or Section 209 of the First General Resolution in any manner which would permit First General Resolution Bonds or Parity Reimbursement Obligations to be issued or incurred which, except for such amendment, could not be issued or incurred; or

(iii) amends Article V of the First General Resolution in any manner which reduces the amount or delays the time at which moneys are to be deposited in the FGR Subordinated Indebtedness Fund or modifies the order in which payments to the FGR Subordinated Indebtedness Fund are to be made or the purposes for which moneys in the FGR Subordinated Indebtedness Fund may be applied; or

(iv) modifies the events which constitute “Events of Default” under Section 1001 of the First General Resolution, or

(v) amends the First General Resolution, the Agreement or the Lease in any manner which would indirectly modify the provisions of any of the Sections of the First General Resolution referred to in clauses (i), (ii), (iii) or (iv) of Section 714(a) of the Resolution in a manner proscribed thereby; or

(vi) adversely affects the interest of the Holders of Outstanding Bonds in any material respect.

No such amendment, change, modification, termination or waiver shall take effect unless the prior written consent of (a) the Holders of at least a majority in principal amount of the Bonds then Outstanding, or (b) in case less than all of the several Series of Bonds then Outstanding are affected by the amendment, change, modification, termination or waiver, the Holders of not less than a majority in principal amount of the Bonds of the Series so affected and then Outstanding; *provided, however*, that if such amendment, change modification, termination or waiver will, by its terms, not take effect so long as any Bonds of any specified Series and maturity remain Outstanding, the consent of the Holders of such Bonds shall not be required and such Bonds shall not be deemed to be Outstanding for the purpose of any calculation of Outstanding Bonds under the provisions contained under this “Amendments to First General Resolution and Agreement.”

Notwithstanding the provisions of the preceding paragraph, the amendments to the First General Resolution made be the resolution of the Authority entitled “Twenty-second Supplemental Resolution to the Water and Sewer System General Revenue Bond Resolution adopted November 14, 1985,” which resolution was adopted by the Authority on November 10, 1993, and any amendments to the Agreement necessary or appropriate to implement or conform the provisions of the Agreement to the First General Resolution as so amended may take effect without the prior written consent of Holders of any of the Bonds.

For the purposes of the provisions under this heading “Amendments to First General Resolution, Agreement and Lease” the purchasers of the Bonds of a Series, whether purchasing as underwriters, for resale or otherwise, upon such purchase from the Authority, may consent to an amendment, change, modification, termination or waiver permitted by the paragraphs under this heading “Amendments to First General Resolution, Agreement and Lease” with the same effect as a consent given by the Holder of such Bonds.

For the purposes of the provisions under this heading, “Amendments to First General Resolution, Agreement and Lease,” Series shall be deemed to be adversely affected by an amendment, change, modification or alteration of the First General Resolution or the Agreement if the same adversely affects or diminishes the rights of the Holders of the Bonds of such Series in any material respect. The Trustee may in its discretion determine whether or not, in accordance with the foregoing provisions, Bonds of any particular Series would be adversely affected in any material respect by any amendment, change, modification or alteration, and any such determination shall be binding and conclusive on the Authority and all Holders of Bonds.

For the purposes of the provisions under this heading “Amendments to First General Resolution, Agreement and Lease,” the Trustee shall be entitled to rely upon an opinion of counsel, which counsel shall be satisfactory to the Trustee with respect to whether any amendment, change, modification or alteration adversely affects the interests of any Holders of Bonds then Outstanding in any material respect. (*Section 714*)

**Supplemental Resolutions.** The Resolution permits the modification or amendment of the rights and obligations of the Authority and of the holders of the Bonds thereunder by a Supplemental Resolution, with the written consent of the holders of a majority of the principal amount of: (i) the Bonds then Outstanding and (ii) in case less than all of the several Series of Bonds then Outstanding are affected by the modification or amendment, of the Bonds of the Series so affected and then Outstanding; however, if such modification or amendment will, by its terms, not take effect so long as any Bonds of any specified like Series and maturity remain Outstanding, the consent of the holders of such Bonds shall not be required and such Bonds shall not be deemed to be Outstanding for the purpose of modification: provided no such modification or amendment shall change the terms of redemption, maturity of principal, installment of interest, or reduce the principal amount, Redemption Price, or rate of interest without the consent of the holder of the affected Bond, or reduce the percentages of consents required to effect any future modification or amendment.

The Authority may adopt (without the consent of any holders of the Bonds) supplemental resolutions to authorize additional Bonds; to add to the restrictions contained in the Resolution upon the issuance of additional indebtedness; to add to the covenants of the Authority contained in, or surrender any rights reserved to or conferred upon it by, the Resolution; to confirm any pledge under the Resolution of Revenues or other moneys; to preserve the federal tax exemption of interest on the Bonds; or otherwise to modify any of the provisions of the Resolution (but no such other modification may be effective while any of the Bonds of any Series theretofore issued are Outstanding); or to cure any ambiguity, supply any omission or to correct any defect in the Resolution or to insert such provisions clarifying matters or questions arising under the Resolution as are necessary or desirable, and are not contrary to or inconsistent with the Resolution as theretofore in effect; or to modify any provision of the Resolution or of any previously adopted Supplemental Resolution in any respect, provided that such modification shall not adversely affect the interests of the Bondholders in any material respect: or to provide for additional duties of the Trustee (provided that the Trustee shall consent thereto).

For the purposes of Article IX of the Resolution, the purchasers of the Bonds of a Series, whether purchasing as underwriters, for resale or otherwise, upon such purchase from the Authority, may consent to a modification or amendment permitted by Sections 803 or 902 of the Resolution in the manner provided in the Resolution, except that no proof of ownership shall be required, and with the same effect as a consent given by the Holder of such Bonds; *provided, however*, that, if such consent is given by a purchaser who is purchasing as an underwriter or for resale, the nature of the modification or amendment and the provisions for the purchaser consenting thereto shall be described in the official statement, prospectus, offering memorandum or other offering document prepared in connection with the primary offering of the Bonds of such Series by the Authority. (*Arts. VIII and IX*)

**Defaults and Remedies.** The Resolution provides that if one or more of the following Events of Default shall occur, namely: (i) a default in the payment of the principal or Redemption Price of any Bond; (ii) a default in payment of any installment of interest on any Bond; (iii) a default by the Authority in the performance or observance of any other of its covenants, agreements or conditions in the Resolution for a period of 45 days after written notice thereof; (iv) a default under the Agreement or the Lease by the Board or the City for a period of 45 days after written notice thereof; (v) a filing of a petition for relief under any federal or State bankruptcy or similar law by the Authority; or (vi) a default by the Authority on any indebtedness payable out of the FGR Subordinated Indebtedness Fund has occurred as a result of which the principal thereof has been declared to be immediately due and payable, which declaration has not been annulled; then, upon the happening and continuance of any Event of Default, the Trustee, if no First General Resolution Bonds are then Outstanding under the First General Resolution or if the principal of all First General Resolution Bonds then Outstanding has been declared to be due and payable immediately pursuant to Section 803 of the First General Resolution, may, and

upon the written request of the holders of not less than a majority in principal amount of the Bonds Outstanding the Trustee shall, declare the principal and accrued interest on all the Bonds then Outstanding, due and payable immediately subject, however, to rescission of such declaration and annulment of the default upon be remedying thereof.

The Authority covenants that upon the occurrence of an Event of Default, the books of record and account of the Authority shall at all times be subject to the inspection and use of the Trustee and of its agents and attorneys and that, upon demand of the Trustee, the Authority will account, as if it were the trustee of an express trust, for all Revenues and other moneys, securities and funds pledged or held under the Resolution for such period as shall be stated in such demand.

Upon default, the Trustee may proceed to protect and enforce its rights and the rights of the holders of the Bonds under the Resolution forthwith by a suit or suits in equity or at law, whether for the specific performance of any covenant therein contained, or in aid of the execution of any power therein granted, or for an accounting against the Authority as if the Authority were the trustee of an express trust, or in the enforcement of any other legal or equitable right as the Trustee, being advised by counsel, shall deem most effectual to enforce any of its rights or to perform any of its duties under the Resolution. During the continuance of an Event of Default, Revenues shall be applied first, to the reasonable and proper charges and expenses of the Trustee; then (unless the principal thereof shall have been declared payable) to the payment of all unpaid interest ratably, and then to unpaid principal or Redemption Price of any Bond or Parity Reimbursement Obligations, ratably; if the principal of all of the Bonds shall be due and payable, to the payment of the principal and interest then due and unpaid upon the Bonds and Parity Reimbursement Obligations and of the interest then due and unpaid on Parity Bond Anticipation Notes without preference or priority of principal over interest or of interest over principal, or of any installment of interest over any other installment of interest, or of any Bond, Parity Reimbursement Obligation or Parity Bond Anticipation Note over any other Bond, Parity Reimbursement Obligation or Parity Bond Anticipation Note, ratably, according to the amounts due respectively for principal and interest, to the persons entitled thereto without any discrimination or preference. No Bondholder has any right to institute a suit to enforce any provision of the Resolution or the execution of any trust thereunder or for any remedy thereunder, unless the Trustee has been requested by the holders of at least a majority in principal amount of the Bonds then Outstanding to take such action and has been offered adequate security and indemnity and has failed to commence such suit in the manner provided in the Resolution. The right to appoint a statutory trustee under Section 1045-p of the Act is expressly abrogated. (*Art. X*)

**Defeasance of Bonds Other than Variable Rate or Option Bonds.** Any Outstanding Bond shall prior to the maturity or redemption date thereof be deemed to have been paid and shall cease to be entitled to any lien, benefit or security under the Resolution if (i) in the case of any Bonds to be redeemed prior to their maturity, the Authority shall have given to the Trustee irrevocable instructions accepted in writing by the Trustee to publish on such date the notice of redemption therefor (other than Bonds purchased by the Trustee prior to the publication of the notice of redemption), (ii) there shall have been deposited with the Trustee either moneys in an amount sufficient, or Defeasance Obligations the principal of and the interest on which, when due, without reinvestment, will, as verified by the report of a firm of nationally recognized independent certified public accountants, provide moneys which, together with the moneys deposited shall be sufficient, to pay when due the principal or Redemption Price (if applicable) and interest due and to become due on said Bonds and (iii) in the event said Bonds are not by their terms subject to redemption within the next succeeding 60 days, the Authority shall have given the Trustee irrevocable instructions to publish, as soon as practicable, a notice to the holders of such Bonds that the deposit required above has been made with the Trustee and that said Bonds are deemed paid in accordance with the Resolution and stating such maturity or redemption date upon which moneys are to be available to pay the principal or Redemption Price, if applicable, on such Bonds (other than Bonds purchased by the Trustee prior to the publication of the notice of redemption); provided that any notice published for Bonds constituting less than all of the Outstanding Bonds of any maturity within a Series shall specify the letter and number or other distinguishing mark of each such Bond. The Trustee shall, to the extent necessary, apply moneys to the retirement of said Bonds in amounts equal to the unsatisfied balances of any Sinking Fund Installments thereto.

The Trustee shall, if so directed by the Authority prior to the maturity date of Bonds deemed to have been paid which are not to be redeemed prior to their maturity date or prior to the publication of the above notice of redemption for Bonds deemed paid and to be redeemed, apply moneys deposited with the Trustee in respect of such Bonds and redeem or sell Defeasance Obligations so deposited with the Trustee and purchase such Bonds and the Trustee shall immediately thereafter cancel all such Bonds so purchased; *provided, however*, that the moneys and Defeasance Obligations remaining on deposit with the Trustee after the purchase and cancellation of such Bonds shall be sufficient to pay when due the Principal Installment or Redemption Price, if applicable, and interest due or to become due on all Bonds. (Section 1201)

**Defeasance of Variable Rate Bonds.** The Resolution provides that for the purposes of determining whether Variable Rate Bonds shall be deemed to have been paid prior to the maturity or redemption date thereof, by the deposit of moneys, or Defeasance Obligations and moneys (if any), the interest due on such Bonds shall be calculated at the maximum rate permitted; *provided, however*, that if, as a result of such Bonds having borne interest at less than the maximum rate for any' period, the total amount of moneys and Investment Securities on deposit with the Trustee for the payment of interest on such Bonds exceeds the total amount required to be deposited with the Trustee, the Trustee shall, if requested by the Authority, pay the amount in excess to the Authority free and clear of any lien or pledge securing the Bonds or otherwise existing under the Resolution. (Section 1201)

**Defeasance of Option Bonds.** Under the Resolution, Option Bonds shall be deemed paid in accordance with the Resolution only if, in addition to satisfying several of the requirements applicable to Bonds other than Variable Rate or Option Bonds, there shall have been deposited with the Trustee moneys in an amount which shall be sufficient to pay the maximum amount of principal of and premium due, if any; and interest on such Bonds which could become payable to the holders of such Bonds upon the exercise of any options provided to the holders of such Bonds; *provided, however*, that if the options originally exercisable by the holder of an Option Bond are no longer exercisable, such Bond shall not be considered an Option Bond. (Section 1201)

### **Summary of the First Resolution**

*Terms used in this Summary of the First Resolution shall have the meanings ascribed thereto in "APPENDIX C—GLOSSARY AND SUMMARY OF CERTAIN DOCUMENTS—Glossary—Definition of Certain Terms Used in First Resolution".*

**Pledge of Revenues and Funds.** The Authority pledges for the payment of the Principal Installments or Redemption Price of and any interest on the Bonds, in accordance with their terms and the provisions of the Resolution: (i) all Revenues, (ii) all moneys or securities in any of the Funds and Accounts created under the Resolution, except that moneys or securities on deposit in a Special Account are pledged only to the Series of Bonds to which such Account relates and moneys or securities on deposit in the Common Account are pledged only to the Bonds for which a Special Account has not been established pursuant to the Resolution, and (iii) all other moneys and securities to be received, held or set aside by the Authority or by any Fiduciary pursuant to the Resolution; subject only to the provisions of the Resolution and the Agreement permitting the application of such amounts for or to the purposes and on the terms and conditions therein set forth. It is the intention of the Authority that, to the fullest extent permitted by law, such pledge shall be valid and binding from the time when it is made; that the Revenues, moneys, securities and other funds so pledged, and then or thereafter received by the Authority, shall immediately be subject to the lien of such pledge; and that the obligation to perform the contractual provisions therein contained shall have priority over any or all other obligations and liabilities of the Authority and shall be valid and binding as against all parties having claims of any kind in tort, contract or otherwise against the Authority, irrespective of whether such parties have notice thereof.

As further security for the payment of the Bonds, the Authority, under the Resolution, assigns, transfers and pledges to the Trustee all of its rights and interests under and pursuant to the Agreement (excluding rights to notice and other procedural rights, its right to indemnification and rights and interests not material to Bondholders), including, without limiting the generality of the foregoing, the present and continuing right: (i) to claim, collect or receive from the Board, all Revenues thereunder, (ii) to bring

actions and proceedings thereunder for enforcement of such right of collection, and (iii) to do any and all things which the Authority is or may become entitled to do under the Agreement; provided that such assignment shall not impair or diminish any obligation of the Authority under the Agreement.

The Bonds are special obligations of the Authority payable solely from the Revenues and other amounts described in the Resolution and do not and will not constitute an indebtedness of the State, the City or the Board and neither the State, the City nor the Board shall be in any way liable thereon. (*Sections 203 and 501*)

**Establishment of Funds and Accounts.** The Resolution establishes the following Funds:

- (1) Construction Fund;
- (2) Revenue Fund;
- (3) Debt Service Fund;
- (4) Authority Expense Fund;
- (5) Debt Service Reserve Fund;
- (6) Subordinated Indebtedness Fund;
- (7) Surplus Fund; and
- (8) Arbitrage Rebate Fund.

The Resolution establishes in the Debt Service Reserve Fund a separate account known as the “Common Account”, and provides that any Supplemental Resolution which authorizes a Special Credit Facility may establish one or more “Special Accounts” in the Debt Service Reserve Fund. The Resolution also establishes in the Debt Service Reserve Fund a separate account to be known as the “Capitalized Interest Account”.

The Trustee shall hold all of the Funds and Accounts, except the Authority Expense Fund, which shall be held by the Authority.

The Trustee is directed to make withdrawals and transfers from the Funds and Accounts established by the Resolution in order to comply with any agreement entered into upon or after the date of issuance of the Authority’s Fiscal 1987 Series C Bonds providing for the rebate of certain arbitrage earnings to the United States. (*Section 502*)

**Construction Fund.** The Authority shall deposit from time to time in the Construction Fund the net proceeds from the sale of each Series of Bonds and make the deposits in the Funds and Accounts required by the applicable Supplemental Resolutions. The Authority shall also deposit from time to time in the Construction Fund any other amounts required to be deposited therein pursuant to the Resolution or the Agreement, including amounts received by the Authority for or in connection with the System and determined by the Authority to be deposited therein. Any proceeds of insurance maintained by the Board or the City against physical loss of or damage to the System, or of contractors’ performance bonds pertaining to the construction of the System, shall also be paid into the Construction Fund.

Except as otherwise provided, amounts in the Construction Fund may only be expended to pay Costs of Water Projects (including Costs of Issuance). The Trustee shall make payments from the Construction Fund, except as otherwise provided, only upon receipt of a Disbursement Request signed by an Authorized Representative of the Authority.

To the extent that other moneys are not available therefor in any other Fund or Account, amounts in the Construction Fund shall be applied to the payment of principal of and interest on Bonds when due. (*Section 503*)

**Allocation of Revenues—Revenue Fund.** The Authority shall cause all Revenues received from the Board pursuant to the Agreement or otherwise to be paid to the Trustee and deposited promptly upon receipt in the Revenue Fund. There shall also be deposited in the Revenue Fund all other amounts required by the Resolution or the Agreement to be so deposited. (*Section 504*)

**Payments Into Certain Funds.** From the Revenues in the Revenue Fund, the Trustee shall make, as soon as practicable in each month, the following deposits in the following order:

(i) to the Debt Service Fund all such amounts until the amount therein on deposit in such month equals the Minimum Monthly Balance for such month for all Series of Bonds Outstanding;

(ii) from the balance, if any, remaining in such month after making the deposits required in (i) above, to the Authority Expense Fund the entire balance until the total on deposit therein in such month is equal to the product obtained by multiplying (A) the sum of the Authority Expenses for the then current Fiscal Year plus (if included in the Authority Budget for the then current Fiscal Year) an amount (the "Reserve for Expenses") equal to one-sixth ( $\frac{1}{6}$ th) of such Authority Expenses by (B) a fraction, the numerator of which is 12 minus the number of full months, excluding the month of calculation, remaining in the Fiscal Year, and the denominator of which is 12;

(iii) from the balance, if any, remaining after making the deposits required in (i) and (ii) above, *first*, to the Common Account in the Debt Service Reserve Fund, the amount, if any, necessary to make the total on deposit in the Common Account equal to the Debt Service Reserve Requirement for the Bonds to which such Common Account relates or, if less than sufficient, the entire balance and, *second*, to each Special Account until the amount therein on deposit equals the Debt Service Reserve Requirement for the Bonds to which each Special Account relates; *provided, however*, if the balance remaining is less than sufficient to credit in full each Special Account, credit shall be made pro rata among all Special Accounts in the same ratio as the Debt Service Reserve Requirement related to such Special Account bears to the sum of the Debt Service Reserve Requirements for all of the Bonds related to the Special Accounts; and

(iv) from the balance, if any, remaining after making the deposits required in (i), (ii) and (iii) above, to the Subordinated Indebtedness Fund the amount required to be deposited in accordance with the Authority Budget, or the entire balance, if less than sufficient.

Beginning with the first day of each Fiscal Year, the Trustee shall calculate the amounts deposited in the Revenue Fund on a daily basis until the total of all amounts deposited therein during such Fiscal Year is at least equal to the Cash Flow Requirement. On such date, if any, the Trustee is directed to give the notice to the Authority and the Board provided in Section 4.3(b) of the Agreement. Thereafter, during each Fiscal Year, no further Revenues shall be paid to the Trustee pursuant to paragraph Fourth of Section 4.2(c) of the Agreement so long as the Cash Flow Requirement, as the same may be revised from time to time, continues to be met. (*Section 505*)

**Debt Service Fund.** The Trustee shall, for each Series of Bonds Outstanding, pay from the Debt Service Fund the amounts due on each Bond Payment Date for the payment of the Principal Installments, if any, and from the moneys in the Debt Service Fund, including moneys in the Capitalized Interest Account in such Fund, interest on the Outstanding Bonds and on the redemption date or date of purchase, the amounts required for the payment of accrued interest on Bonds to be redeemed or purchased on such date unless the payment of such accrued interest shall be otherwise provided.

The Trustee may, and if so directed by an Authorized Representative of the Authority shall, prior to the forty-fifth day preceding the due date of each Sinking Fund Installment, apply the amounts accumulated in the Debt Service Fund for such Sinking Fund Installment, together with any interest on the Bonds for which such Sinking Fund Installment was established: (i) to the purchase of Bonds of like Series and maturity at prices (including any brokerage and other charges) not exceeding the Redemption Price payable for such Bonds when such Bonds are redeemable with such Sinking Fund Installment plus unpaid interest accrued or (ii) to the redemption of such Bonds, if redeemable by their terms, at or below said Redemption Price. Upon such purchase or redemption of any Bond, the Trustee shall then credit an amount equal to the principal of the Bond so purchased or redeemed toward the next Sinking Fund Installments thereafter to become due and the amount of any excess over the amount of such Sinking Fund Installment shall be credited against future Sinking Fund Installments in direct chronological order.

In any event, the Trustee shall, as soon as practicable after the forty-fifth day preceding the due date of any such Sinking Fund Installment, call for redemption a sufficient amount of Bonds of like Series and

maturity to complete the retirement of the principal amount specified for such Sinking Fund Installment of such Bonds whether or not it then has moneys in the Debt Service Fund to pay the applicable Redemption Price thereof on the redemption date. The Trustee shall apply to the redemption of the Bonds on each such redemption date the amount required for the redemption of such Bonds. *(Sections 506 and 514)*

**Authority Expense Fund.** The Authority shall apply amounts credited to the Authority Expense Fund to the payment of Authority Expenses. Any moneys in the Authority Expense Fund which the Authority determines are in excess of that needed to meet the sum of the unpaid Authority Expenses for such Fiscal Year plus (if such amount was included in the Authority Budget for such Fiscal Year) the Reserve for Expenses, shall be applied toward any deficiencies in the following Funds and Accounts in the order stated: the Debt Service Fund, Debt Service Reserve Fund and Subordinated Indebtedness Fund. Any remaining amounts shall be credited to the Revenue Fund. *(Section 507)*

**Debt Service Reserve Fund.** The Resolution establishes a Debt Service Reserve Fund and a Common Account therein. In addition, the Resolution provides that any Supplemental Resolution which provides for a Special Credit Facility to secure the principal, interest or Tender Option Price of any Bonds may establish one or more "Special Accounts" in the Debt Service Reserve Fund. From the proceeds of each Series of Bonds there shall be deposited in the Debt Service Reserve Fund the amount, if any, necessary to make the amount on deposit therein equal to the Debt Service Reserve Requirement, after giving effect to the issuance of such Bonds; and all such amounts will be credited to the Common Account, unless a Supplemental Resolution requires a deposit in a Special Account. Amounts on deposit in the Common Account will be applied, to the extent necessary, to pay the Principal Installments of and interest on the Bonds; *provided, however,* that the amounts in the Common Account may not be applied to pay the Principal Installments or Tender Option Price of or interest on Bonds for which such payments are secured by a Special Credit Facility, if the Supplemental Resolution authorizing such Bonds has established a Special Account. Likewise, amounts in any Special Account may not be applied to pay the Principal Installments of or interest on any Bond for which such payments may be made from the Common Account. Amounts on deposit in each of the Accounts in the Debt Service Reserve Fund shall be applied, to the extent other funds are not available in the Surplus Fund, the Subordinated Indebtedness Fund and the Authority Expense Fund, to pay the Principal Installments of, and interest on the Bonds to which such Account relates when due. Amounts so applied shall be derived first from cash or Investment Securities on deposit, and second from draws and demands on Financial Guaranties.

If, as of June 30 of each year, the amount in any Account in the Debt Service Reserve Fund exceeds the applicable Debt Service Reserve Requirement after giving effect to any Financial Guaranty deposited in such Fund, the Trustee shall, on the first business day of the following Fiscal Year, withdraw from such Account the amount of any excess therein over the applicable Debt Service Reserve Requirement as of the date of such withdrawal for deposit into (i) the Arbitrage Rebate Fund, the amount estimated by the Authority to be required by the Code to be rebated to the Department of the Treasury, (ii) the Surplus Fund, the amount required to be deposited therein in accordance with the Authority Budget, and (iii) the Revenue Fund, the amount of any excess then remaining in the Debt Service Reserve Fund over the applicable Debt Service Reserve Fund Requirement.

Whenever the amount (exclusive of Financial Guaranties) in all of the Accounts in the Debt Service Reserve Fund, together with the amount in the Debt Service Fund, is sufficient to pay all Outstanding Bonds in accordance with their respective terms, the funds on deposit in the Debt Service Reserve Fund shall be transferred to the Debt Service Fund and applied to the redemption or payment at maturity of all Bonds Outstanding.

In lieu of the required deposits and transfers to the Debt Service Reserve Fund, the Authority may cause to be deposited into the Debt Service Reserve Fund Financial Guaranties in an amount equal to the difference between the Debt Service Reserve Requirement and the sums, if any, then on deposit in the Debt Service Reserve Fund or being deposited in the Debt Service Reserve Fund concurrently with such Financial Guaranties. The Financial Guaranties shall be payable (upon the giving of notice as required thereunder) on any date on which moneys will be required to be withdrawn from the Debt Service



Reserve Account and applied to the payment of a Principal Installment of or interest on any Bonds and such withdrawal cannot be met by amounts on deposit in the Debt Service Reserve Fund. If a disbursement is made pursuant to Financial Guaranties, the Authority shall be obligated either (i) to reinstate the maximum limits of such Financial Guaranties or (ii) to deposit into the Debt Service Reserve Fund, funds in the amount of the disbursement made under such Financial Guaranties, or a combination of such alternatives, as shall provide that the amount in the Debt Service Reserve Fund equals the Debt Service Reserve Requirement.

In the event of the refunding of any Bonds, the Trustee shall, upon the written direction of the Authority, withdraw from the Debt Service Reserve Fund all or any portion of amounts accumulated therein with respect to the Bonds being refunded and deposit such amounts as provided in such written direction; provided that such withdrawal shall not be made unless (a) immediately thereafter the Bonds being refunded shall be deemed to have been paid pursuant to Section 1201 of the Resolution, and (b) the amount remaining in the Debt Service Reserve Fund after such withdrawal shall not be less than the Debt Service Reserve Requirement. (*Section 508*)

**Subordinated Indebtedness Fund.** The Trustee shall apply amounts on deposit in the Subordinated Indebtedness Fund solely to the maintenance of reserves for, or the payment of, Subordinated Indebtedness (or as otherwise provided by the resolution of the Authority authorizing each issue of Subordinated Indebtedness). The Trustee shall withdraw from the Subordinated Indebtedness Fund any amount necessary to render the balances in the Debt Service Fund or Debt Service Reserve Fund sufficient to meet the requirements of such Funds. (*Section 509*)

**Surplus Fund.** The Trustee shall, on each Bond Payment Date, apply moneys credited to the Surplus Fund in the following amounts: (i) to the Debt Service Fund the amount, if any, necessary (or all the moneys in the Surplus Fund if less than the amount necessary) to make up any deficiency in the amount required to be on deposit in such Fund and (ii) to the Debt Service Reserve Fund the amount, if any, necessary (or all the moneys in the Surplus Fund if less than the amount necessary) to make up any deficiency in the amount required to be on deposit in any Account in such Fund. Such transfer shall be made notwithstanding any other provisions of this Resolution requiring deposits in such Funds. Amounts on deposit in the Surplus Fund on the last day of a Fiscal Year shall be withdrawn from such Fund and transferred to the Board for deposit in the Local Water Fund. (*Section 510*)

**Arbitrage Rebate Fund.** Amounts on deposit in the Arbitrage Rebate Fund shall be applied by the Trustee to make payments to the Department of the Treasury of the United States of America. Notwithstanding the foregoing, the Trustee shall apply moneys credited to the Arbitrage Rebate Fund in the following amounts: (i) to the Debt Service Fund the amount, if any, necessary (or all the moneys in the Arbitrage Rebate Fund if less than the amount necessary) to make up any deficiency in the amount required to be on deposit in the Debt Service Fund and (ii) to the Debt Service Reserve Fund the amount, if any, necessary (or all the moneys in the Arbitrage Rebate Fund if less than the amount necessary) to make up any deficiency in the amount required to be on deposit in any Account in the Debt Service Reserve Fund.

Amounts on deposit in the Arbitrage Rebate Fund in excess of the amount required to be maintained therein for the purposes of such Fund may be transferred and paid by the Trustee to the Surplus Fund. (*Section 510-a*)

**Subordinated Indebtedness.** The Authority may issue Subordinated Indebtedness payable out of and secured by a pledge of and lien on amounts in the Subordinated Indebtedness Fund available for such payment. Such Subordinated Indebtedness, however, shall be issued only for the purposes set forth in the Resolution and shall be secured by a pledge subordinate in all respects to the pledge created by the Resolution as security for the Bonds. (*Section 511*)

**Depositaries.** All moneys or securities held by the Trustee shall constitute trust funds and the Trustee may and shall, if directed by the Authority, deposit such moneys or securities with one or more Depositaries. All moneys or securities held by the Authority in the Authority Expense Fund shall be

deposited with one or more Depositaries. All moneys or securities deposited under the provisions of the Resolution with the Trustee or any Depositary shall be held in trust and applied only in accordance with the provisions of the Resolution, and each of the Funds established by the Resolution shall be a trust fund for the purposes thereof.

Each Depositary holding moneys or securities in trust for the Trustee shall be a bank or trust company organized under the laws of the State or a national banking association (having its principal office within the State), having capital stock, surplus and undivided earnings aggregating at least \$100,000,000 and willing and able to accept the office on reasonable and customary terms and authorized by law to act in accordance with the provisions of the Resolution. (*Section 512*)

**Investment of Certain Funds.** Moneys held in the Debt Service Fund, the Debt Service Reserve Fund and the Subordinated Indebtedness Fund (subject to the terms of any resolutions or other instruments securing any issue of Subordinated Indebtedness) shall be invested and reinvested to the fullest practicable extent in Investment Securities which mature not later than such times as shall be necessary to provide moneys when needed to make payments required from such Funds; provided that in the case of the Debt Service Reserve Fund maturation may not occur later than fifteen years from the date of such investment, and in the case of the Debt Service Fund, investments shall be of the type described in clauses (ii), (iii) and (vi), and in the case of the Debt Service Reserve Fund, clauses (ii) and (iii), of the definition of "Investment Securities" (in either case, to the fullest extent practicable). Moneys in the Authority Expense Fund, the Revenue Fund, the Construction Fund, the Arbitrage Rebate Fund and the Surplus Fund may be invested in Investment Securities which mature no later than such times as shall be necessary to provide moneys when needed to make payments from such Funds. The Trustee shall make all investments in accordance with written instructions from any Authorized Representative of the Authority. Moneys in any Fund or Account may be combined with moneys in any other Fund or Account for the purpose of making such investments in Investment Securities.

Interest (net of that which represents a return of accrued interest paid in connection with the purchase of any investment) earned on any moneys or investments in such Funds and Accounts, other than the Construction Fund, the Arbitrage Rebate Fund and the Debt Service Reserve Fund, shall be paid into the Revenue Fund as and when received. Interest (net of that which represents a return of accrued interest paid in connection with the purchase of any investment) earned on any moneys or investments in (i) the Debt Service Reserve Fund shall be paid into the Arbitrage Rebate Fund or the Surplus Fund, (ii) the Construction Fund shall be paid to the Board for deposit in the Local Water Fund quarterly, on the 15th day of each July, October, January and April of each Fiscal Year upon receipt of a written request and a certificate of the Authority relating to the satisfaction of the Cash Flow Requirement and (iii) the Arbitrage Rebate Fund shall remain in such fund.

All Investment Securities acquired with moneys in any Fund or Account, including any Fund or Account held by the Authority, shall be held by the Trustee in pledge or by a Depositary as agent in pledge in favor of the Trustee. (*Section 514*)

**Additional Bonds.** The Authority may issue Bonds from time to time without limitation as to amount except as provided in the Resolution or as specified by law to generate funds sufficient to meet the Costs of Water Projects, to make deposits in the Funds and Accounts or to refund Outstanding Bonds, Bond Anticipation Notes, Subordinated Indebtedness or outstanding bonds of the City issued to pay the capital costs of the System. All Bonds shall be issued subject to the terms, conditions and limitations established in the Resolution and in one or more Series as therein provided.

Bonds shall be authenticated and delivered only upon the Trustee's receipt of, among other items:

- (a) a certified copy of the Supplemental Resolution authorizing such Series;
- (b) (i) in the case of the initial Series of Bonds, an executed copy of the Agreement and the Lease; and (ii) in the case of any subsequent Series of Bonds, an executed copy of any amendment or supplement to the Agreement or the Lease not theretofore delivered to the Trustee;
- (c) except in the case of Series of Bonds issued prior to July 1, 1986 and any Series of Refunding Bonds issued pursuant to Section 207 of the Resolution, a certificate of an Authorized Representa-

tive of the Authority setting forth (i) the Revenues for either of the last two full Fiscal Years immediately preceding the Fiscal Year in which such Bonds are to be issued and (ii) the Aggregate Debt Service during such Fiscal Year for which Revenues are set forth pursuant to clause (i) above (excluding from Aggregate Debt Service any Principal Installment or portion thereof which was paid from sources other than Revenues) and (iii) the sum of the Operating Expenses and the Required Deposits for such period, and showing that the amount set forth in (i) is at least equal to the sum of (x) an amount equal to 115% of the amount set forth in (ii) and (y) an amount equal to 100% of the amount set forth in (iii);

(d) except in the case of the initial Series of Bonds under the Resolution and any Series of Refunding Bonds issued pursuant to Section 207 of the Resolution, a certificate of the Consulting Engineer setting forth the projected Operating Expenses for each of the five Fiscal Years following the Issuance of such Series of Bonds (plus the Fiscal Year in which such Bonds are issued);

(e) except in the case of the initial Series of Bonds under the Resolution and any Series of Refunding Bonds issued pursuant to Section 207, a certificate, signed by an Authorized Representative of the Authority setting forth the estimated Required Deposits for each of the five Fiscal Years following the issuance of such Series of Bonds (plus the Fiscal Year in which such Bonds are issued); and

(f) except in the case of the initial Series of Bonds under the Resolution and any Series of Refunding Bonds issued pursuant to Section 207, a certificate of the Rate Consultant (i) setting forth the estimated Revenues for each of the five Fiscal Years following the issuance of such Series of Bonds (plus the Fiscal Year in which such Bonds are issued) after giving effect to any increases or decreases in rates, fees and charges projected for such Fiscal Years and (ii) showing for each such Fiscal Year that the estimated Revenues for such Fiscal Year will be at least equal to the sum of (A) 115% of the maximum estimated Adjusted Aggregate Debt Service on all Bonds then Outstanding including the Bonds to be issued, and (B) 100% of the sum of the projected Operating Expenses and Required Deposits, as shown on the Certificate of the Consulting Engineer delivered pursuant to paragraph (e) above and the Certificate of the Authority delivered pursuant to paragraph (f) above, respectively. (*Sections 204 and 206*)

**Refunding Bonds.** One or more Series of Refunding Bonds may be issued pursuant to Section 207 of the Resolution at any time to refund any Outstanding Bonds provided that (i) estimated average annual Debt Service on such Series of Refunding Bonds shall not exceed the average annual Debt Service on the Bonds to be refunded and (ii) the maximum Debt Service in any Fiscal Year on such Series of Refunding Bonds shall not exceed the maximum Debt Service in any Fiscal Year on the Bonds to be refunded, all as shown in a Certificate signed by an Authorized Representative of the Authority and delivered to the Trustee prior to the authentication and delivery of such Series of Refunding Bonds. Refunding Bonds shall be issued in a principal amount sufficient, together with other moneys available therefor, to accomplish such refunding and to make the deposits in the Funds and Accounts required by the provisions of the Supplemental Resolution authorizing such Bonds. (*Section 207*)

**Bond Anticipation Notes.** Whenever the Authority shall authorize the issuance of a Series of Bonds, the Authority may, by resolution, authorize the issuance of notes (and renewals thereof) in anticipation of such Series of Bonds. The principal of and interest on such notes and renewals thereof shall be payable from the proceeds of such notes or from the proceeds of the sale of the Series of Bonds in anticipation of which such notes are issued. The proceeds of such Bonds may be pledged for the payment of the principal of and interest on such notes and any such pledge shall have a priority over any other pledge of such proceeds created by the Resolution. The Authority may also pledge the Revenues to the payment of the interest on, and subject to Section 707 of the Resolution, the principal of such notes. A copy of the Resolution of the Authority authorizing such notes, certified by an Authorized Representative of the Authority, shall be delivered to the Trustee following its adoption, together with such other information concerning such notes as the Trustee may reasonably request. (*Section 208*)

**Credit Facilities.** In connection with the issuance of any Series of Bonds, the Authority may obtain or cause to be obtained one or more Credit Facilities providing for payment of all or a portion of the

Principal Installments, or Redemption Price or interest due or to become due on such Bonds, providing for the purchase of such Bonds by the issuer of such Credit Facility or providing funds for the purchase of such Bonds by the Authority.

The Authority may secure such Credit Facility by an agreement providing for the purchase of the Series of Bonds secured thereby with such adjustments to the rate of interest, method of determining interest, maturity or redemption provisions as specified by the Authority in the applicable Supplemental Resolution. The Authority may also in an agreement with the issuer of such Credit Facility agree to directly reimburse such issuer for amounts paid under the terms of such Credit Facility, together with interest thereon (the "Reimbursement Obligation"); *provided, however*, that no Reimbursement Obligation shall be created until amounts are paid under such Credit Facility. Any such Reimbursement Obligation (a "Parity Reimbursement Obligation") may be secured by a pledge of, and a lien on Revenues on a parity with the lien created by Section 501 of the Resolution. Upon the payment of amounts under the Credit Facility which payment results in the Parity Reimbursement Obligation becoming due and payable, such Parity Reimbursement Obligation shall be deemed to be part of the Series of Bonds to which the Credit Facility which gave rise to such Parity Reimbursement Obligation relates.

Any such Credit Facility shall be for the benefit of and secure such Series of Bonds or portion thereof, as specified in the applicable Supplemental Resolution. (*Section 209*)

**Indebtedness and Liens.** The Resolution provides that the Authority shall not issue any bonds, or other evidences of indebtedness, other than the Bonds, Bond Anticipation Notes, Subordinated Indebtedness and Parity Reimbursement Obligations, secured by a pledge of or other lien on the Revenues and shall not create or cause to be created any lien on such Revenues or on any amounts held by any Fiduciary, under the Resolution; however, the Authority may: (i) issue notes payable from the proceeds of Bonds or other obligations for the corporate purposes of the Authority payable or secured by Revenues derived on and after such date as the pledge of the Revenues provided in the Resolution is discharged and satisfied and (ii) issue bonds or other obligations for the corporate purposes of the Authority payable out of or secured by the pledge of amounts in the Local Water Fund after satisfaction of the Cash Flow Requirement for the then current Fiscal Year, and which recite on their face that such pledge of said amounts is and shall be in all respects subordinate to the provisions of the lien and pledge created by the Resolution. (*Section 707*)

**Agreement of the State.** In accordance with Section 1045-t of the Act, the Authority agrees, for and on behalf of the State, that the State will not alter or limit the rights vested by the Act in the Authority or the Board to fulfill the terms of any agreement made with or for the benefit of the Bondholders, or in any way impair the rights and remedies of Bondholders, until the Bonds, together with the interest thereon, with interest on any unpaid installment of interest, and all costs and expenses in connection with any action or proceeding by or on behalf of such holders, are fully met and discharged. (*Section 711*)

**Authority Budget.** The Authority shall, on or before May 1, in each Fiscal Year, adopt and file with the Trustee, the Board and the City, a certified copy of the Authority Budget showing the estimated Cash Flow Requirement and the components thereof (on a monthly basis) for the ensuing Fiscal Year, together with any other information required to be set forth therein by the Resolution or the Agreement. Such Authority Budget may set forth such additional information as the Authority may determine or as the Board or the City may request. If for any reason the Authority shall not have adopted the Authority Budget before such May 1, the Authority Budget for the then current Fiscal Year shall be deemed to be the Authority Budget for the ensuing Fiscal Year until a new Authority Budget is adopted. The Authority may at any time adopt an amended Authority Budget for the then current or ensuing Fiscal Year, but no such amended Authority Budget shall supersede any prior Budget until the Authority shall have filed with the Trustee, the Board and the City a copy of such amended Authority Budget. Each month the Authority shall recalculate the Cash Flow Requirement. (*Sections 712 and 713*)

**Enforcement and Amendment of Agreement and Lease.** The Authority shall enforce or cause to be enforced the provisions of the Agreement and the Lease and duly perform its covenants and agreements under the Agreement. The Authority will not consent or agree to or permit any rescission of or amendment to or otherwise take any action under or in connection with the Agreement or the Lease except in accordance with Article X of the Agreement of the Resolution. (*Section 714*)

**Supplemental Resolutions.** The Resolution permits the modification or amendment of the rights and obligations of the Authority and of the holders of the Bonds thereunder by a Supplemental Resolution, with the written consent of the holders of two-thirds of the principal amount of: (i) the Bonds then Outstanding and (ii) in case less than all of the several Series of Bonds then Outstanding are affected by the modification or amendment, of the Bonds of the Series so affected and then Outstanding; however, if such modification or amendment will, by its terms, not take effect so long as any Bonds of any specified like Series and maturity remain Outstanding, the consent of the holders of such Bonds shall not be required and such Bonds shall not be deemed to be Outstanding for the purpose of modification; provided no such modification or amendment shall change the terms of redemption, maturity of principal, installment of interest, or reduce the principal amount, Redemption Price, or rate of interest without the consent of the holder of the affected Bond, or reduce the percentages of consents required to effect any future modification or amendment.

The Authority may adopt (without the consent of any holders of the Bonds) supplemental resolutions to authorize additional Bonds; to add to the restrictions contained in the Resolution upon the issuance of additional indebtedness; to add to the covenants of the Authority contained in, or surrender any rights reserved to or conferred upon it by, the Resolution; to confirm any pledge under the Resolution of Revenues or other moneys; to preserve the federal tax exemption of interest on the Bonds; or otherwise to modify any of the provisions of the Resolution (but no such other modification may be effective while any of the Bonds of any Series theretofore issued are Outstanding); or to cure any ambiguity, supply any omission or to correct any defect in the Resolution or to insert such provisions clarifying matters or questions arising under the Resolution as are necessary or desirable, and are not contrary to or inconsistent with the Resolution as theretofore in effect or to provide for additional duties of the Trustee (provided that the Trustee shall consent thereto). (*Arts. VIII and IX*)

**Defaults and Remedies.** The Resolution provides that if one or more of the following Events of Default shall occur, namely: (i) a default in the payment of the principal or Redemption Price of any Bond; (ii) a default in payment of any installment of interest on any Bond; (iii) a default by the Authority in the performance or observance of any other of its covenants, agreements or conditions in the Resolution for a period of 45 days after written notice thereof; (iv) a default under the Agreement or the Lease by the Board or the City for a period of 45 days after written notice thereof; or (v) a filing of a petition for relief under any federal or State bankruptcy or similar law by the Authority; then, upon the happening and continuance of any Event of Default, the Trustee may, and upon the written request of the holders of not less than a majority in principal amount of the Bonds Outstanding the Trustee shall, declare the principal and accrued interest on all the Bonds then Outstanding, due and payable immediately subject, however, to rescission of such declaration and annulment of the default upon the remedying thereof.

The Authority covenants that upon the occurrence of an Event of Default, the books of record and account of the Authority shall at all times be subject to the inspection and use of the Trustee and of its agents and attorneys and that, upon demand of the Trustee, the Authority will account, as if it were the trustee of an express trust, for all Revenues and other moneys, securities and funds pledged or held under the Resolution for such period as shall be stated in such demand.

Upon default, the Trustee may proceed to protect and enforce its rights and the rights of the holders of the Bonds under the Resolution forthwith by a suit or suits in equity or at law, whether for the specific performance of any covenant therein contained, or in aid of the execution of any power therein granted, or for an accounting against the Authority as if the Authority were the trustee of an express trust, or in the enforcement of any other legal or equitable right as the Trustee, being advised by counsel, shall deem most effectual to enforce any of its rights or to perform any of its duties under the Resolution. During the continuance of an Event of Default, Revenues shall be applied first, to the reasonable and proper charges and expenses of the Trustee; then (unless the principal of all of the Bonds shall have been declared payable) to the payment of all unpaid interest ratably, and then to unpaid principal or Redemption Price, ratably; and if all of the principal of the Bonds shall be due and payable, to the payment of unpaid principal and interest, without preference or priority of interest over principal, principal over interest or of any Bond or installment over any other Bond or installment, without any discrimination or preference. No Bondholder has any right to institute suit to enforce any provision of the Resolution or the execution of any trust thereunder or for any remedy thereunder, unless the Trustee has been requested by the

holders of at least a majority in principal amount of the Bonds to take such action and has been offered adequate security and indemnity and has failed to commence such suit in the manner provided in the Resolution. The right to appoint a statutory trustee under Section 1045-p of the Act is expressly abrogated. (*Art. X*)

**Defeasance of Bonds Other than Variable Rate or Option Bonds.** Any Outstanding Bond shall prior to the maturity or redemption date thereof be deemed to have been paid and shall cease to be entitled to any lien, benefit or security under the Resolution if (i) in the case of any Bonds to be redeemed prior to their maturity, the Authority shall have given to the Trustee irrevocable instructions accepted in writing by the Trustee to publish on such date the notice of redemption therefor (other than Bonds purchased by the Trustee prior to the publication of the notice of redemption), (ii) there shall have been deposited with the Trustee either moneys in an amount sufficient, or Defeasance Obligations the principal of and/or the interest on which, when due, without reinvestment, will, as verified by the report of a firm of nationally recognized independent certified public accountants, provide moneys which, together with the moneys deposited shall be sufficient, to pay when due the principal or Redemption Price (if applicable) and interest due and to become due on said Bonds and (iii) in the event said Bonds are not by their terms subject to redemption within the next succeeding 60 days, the Authority shall have given the Trustee irrevocable instructions to publish, as soon as practicable, a notice to the holders of such Bonds that the deposit required above has been made with the Trustee and that said Bonds are deemed paid in accordance with the Resolution and stating such maturity or redemption date upon which moneys are to be available to pay the principal or Redemption Price, if applicable, on such Bonds (other than Bonds purchased by the Trustee prior to the publication of the notice of redemption); provided that any notice published for Bonds constituting less than all of the Outstanding Bonds of any maturity within a Series shall specify the letter and number or other distinguishing mark of each such Bond. The Trustee shall, to the extent necessary, apply moneys to the retirement of said Bonds in amounts equal to the unsatisfied balances of any Sinking Fund Installments thereto.

The Trustee shall, if so directed by the Authority prior to the maturity date of Bonds deemed to have been paid which are not to be redeemed prior to their maturity date or prior to the publication of the above notice of redemption for Bonds deemed paid and to be redeemed, apply moneys deposited with the Trustee in respect of such Bonds and redeem or sell Defeasance Obligations so deposited with the Trustee and purchase such Bonds and the Trustee shall immediately thereafter cancel all such Bonds so purchased; *provided, however*, that the moneys and Defeasance Obligations remaining on deposit with the Trustee after the purchase and cancellation of such Bonds shall be sufficient to pay when due the Principal Installment or Redemption Price, if applicable, and interest due or to become due on all Bonds. (*Section 1201*)

**Defeasance of Variable Rate Bonds.** The Resolution provides that for the purposes of determining whether Variable Rate Bonds shall be deemed to have been paid prior to the maturity or redemption date thereof, by the deposit of moneys, or Defeasance Obligations and moneys (if any), the interest due on such Bonds shall be calculated at the maximum rate permitted; *provided, however*, that if, as a result of such Bonds having borne interest at less than the maximum rate for any period, the total amount of moneys and Investment Securities on deposit with the Trustee for the payment of interest on such Bonds exceeds the total amount required to be deposited with the Trustee, the Trustee shall, if requested by the Authority, pay the amount in excess to the Authority free and clear of any lien or pledge securing the Bonds or otherwise existing under the Resolution. (*Section 1201*)

**Defeasance of Option Bonds.** Under the Resolution, Option Bonds shall be deemed paid in accordance with the Resolution only if, in addition to satisfying several of the requirements applicable to other than Variable Rate or Option Bonds, there shall have been deposited with the Trustee moneys in an amount which shall be sufficient to pay the maximum amount of principal of and premium due, if any, and interest on such Bonds which could become payable to the holders of such Bonds upon the exercise of any options provided to the holders of such Bonds; *provided, however*, that if the options originally exercisable by the holder of an Option Bond are no longer exercisable, such Bond shall not be considered an Option Bond. (*Section 1201*)

**FINANCIAL STATEMENTS**

**FISCAL YEAR 2004 AUDITED FINANCIAL STATEMENTS OF  
THE NEW YORK CITY WATER AND SEWER SYSTEM**

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## Report of Independent Certified Public Accountants

To the Members of the Boards of  
New York City Municipal Water Finance Authority  
and the New York City Water Board

We have audited the accompanying balance sheets, statements of revenues, expenses and changes in net assets, and cash flows of the business-type activities, the New York City Municipal Water Finance Authority and the New York City Water Board, which collectively comprise the New York City Water and Sewer System (“the System”), a component unit of the City of New York, New York, as of and for the year ended June 30, 2004, which collectively comprise the basic financial statements of the System. These financial statements are the responsibility of the System’s management. Our responsibility is to express an opinion on these financial statements based on our audit. The 2003 summarized comparative financial information of the System was derived from the System’s 2003 financial statements which were audited by other auditors. Those auditors expressed an unqualified opinion on those financial statements in their report dated October 23, 2003. As discussed in Note 14, the System has restated its 2003 financial statements, including beginning balances, during the current year to adjust capital assets, in conformity with accounting principles generally accepted in the United States of America. The other auditors reported on the 2003 financial statements before the restatement.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America as established by the Auditing Standards Board of the American Institute of Certified Public Accountants. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the System’s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities, the New York City

Municipal Water Finance Authority and the New York City Water Board of the System as of June 30, 2004, and the respective changes in its financial position and cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The financial statements include summarized 2003 comparative information. Such information does not include all of the information required to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the System’s financial statements for the year ended June 30, 2003, from which such summarized information was derived.

As discussed above, the financial statements of the System as of and for the year ended June 30, 2003, were audited by other auditors. As discussed in Note 14, these financial statements have been restated. We audited the adjustments described in Note 14 to the financial statements that were applied to restate the 2003 financial statements, including beginning balances, from which the accompanying 2003 summarized financial information was derived. In our opinion, such adjustments are appropriate and have been properly applied. However, we were not engaged to audit, review, or apply any procedures to the 2003 financial statements or summarized financial information of the System other than with respect to such adjustments and, accordingly, we do not express an opinion or any other form of assurance on the 2003 financial statements or summarized financial information taken as a whole.

The accompanying management’s discussion and analysis is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.



New York, New York  
October 25, 2004

## Management's Discussion and Analysis

**OVERVIEW OF THE FINANCIAL STATEMENTS**

The following is an overview of the financial activities of the New York City Water and Sewer System (the System) for the fiscal years ended June 30, 2004 and 2003.

The basic financial statements of the System, which include the balance sheets, the statements of revenues, expenses and changes in net assets and the statements of cash flows, are presented to display information about the reporting entity as a whole, in accordance with Governmental Accounting Standards Board (GASB) Statement No. 34, Basic Financial Statements and Managements Discussion and Analysis for State and Local Governments as amended by

GASB Statement No. 37, Basic Financial Statements and Managements Discussion and Analysis — for State and Local Governments: Omnibus. The statements are prepared using the economic resources measurement focus and the accrual basis of accounting.

The 2003 financial statements have been restated, from the amounts previously reported, to reflect adjustments to utility plant in service and utility plant construction. These adjustments are described further in the capital assets section of this discussion and analysis and in footnote 14 to the financial statements.

**FINANCIAL ANALYSIS AND RESULTS OF OPERATIONS**

The following summarizes the activities of the System for the years 2004 and 2003.

(in thousands)	2004	2003
Revenues:		
Water supply and distribution	\$ 713,097	690,093
Sewer collection and treatment	984,753	952,985
Other operating revenues	75,283	68,842
Total operating revenues	<u>1,773,133</u>	<u>1,711,920</u>
Subsidy Income	68,311	65,816
Investment income	86,949	96,236
Total revenues	<u>1,928,393</u>	<u>1,873,972</u>
Expenses:		
Operations and maintenance	933,736	875,762
Bad debt expense	116,108	89,400
Administration and general	19,853	15,181
Depreciation and amortization	451,585	389,626
Loss on retirement of fixed assets	25,214	—
Interest expense	612,054	584,347
Total expenses	<u>2,158,550</u>	<u>1,954,316</u>
Net loss before capital contributions	(230,157)	(80,344)
Capital contributions	29,875	7,233
Change in net assets	<u>(200,282)</u>	<u>(73,111)</u>
Net Assets — beginning	3,754,465	3,827,576
Net Assets — ending	<u>\$3,554,183</u>	<u>3,754,465</u>

Total operating revenues increased by 3.6% on a rate increase of 5.5%. Water consumption declined by 1.5 % over the year.

The following summarizes other operating revenues:

(in thousands)	2004	2003
Upstate water fees	\$ 24,611	22,790
Late payment fees	41,767	38,235
Connection fees & permits	8,905	7,817
Total other revenues	<u>\$ 75,283</u>	<u>68,842</u>

## Management's Discussion and Analysis

Investment income decreased by 9.7%. The Authority had \$5.7 million in arbitrage rebates in 2004 which are netted against investment income. Total investments decreased by \$300 million.

Total operations and maintenance expense increased by \$58 million or 6.6%. Expenses for operations of the system increased by \$44 million and the rental payment to the City for debt service increased by \$14 million. The two major components of the increase in operations and maintenance were increased costs of \$17 million for upstate watershed protection, and an increase of \$12 million in judgments and

claims. The rental payment increased primarily due to higher debt service payments coming due on bonds issued by New York City prior to the inception of the System.

Bad debt expense increased by \$27 million. The system continues to evaluate the accounts receivable balances and where required deem uncollectible accounts to be written off to bad debt expense.

Interest expense increased by \$28 million or 4.7%. The total debt of the System has increased by \$550 million or 4% and interest expense has increased by nearly the same percentage.

On the balance sheet, the changes in assets, liabilities and net assets are summarized as follows:

(in thousands)	2004	2003
Current unrestricted assets	\$ 458,454	506,598
Current restricted assets	1,964,855	2,272,548
Capital assets	15,174,128	14,163,830
Total assets	<u>17,709,977</u>	<u>17,054,770</u>
Long-term liabilities	12,565,882	11,894,966
Current liabilities	1,589,912	1,405,339
Total liabilities	<u>14,155,794</u>	<u>13,300,305</u>
Net assets:		
Invested in capital assets, net of related debt	3,368,355	3,271,440
Restricted for debt service	179,106	203,695
Restricted for operations & maintenance	135,701	132,107
Unrestricted (deficit)	(128,979)	147,223
Total net assets	<u>3,554,183</u>	<u>3,754,465</u>
Total liabilities and net assets	<u>\$17,709,977</u>	<u>17,054,770</u>

## Management's Discussion and Analysis

Current unrestricted assets decreased by \$48 million or 9.5%. Net receivables including unbilled revenues decreased by \$32 million and the System's receivable from the City for over payment of operations and maintenance expense decreased from 2003 by \$10 million.

Current restricted assets decreased \$308 million or 14%. The major decrease in restricted assets was \$267 million in the construction fund. The balances in this fund are available to pay for capital projects and vary due to the timing of the reissuance of commercial paper following the issue of long term bonds. In 2004 \$40 million in principal payments were made from the escrow funds.

Capital assets are described in a separate section of this discussion.

In 2004, the System issued an additional \$100 million of commercial paper and terminated \$125 million which brought the total program amount to \$800 million. Current liabilities increased by \$184 million primarily due to an increase in payable to the City of \$219 million. Total commercial paper outstanding decreased by \$25 million.

Long-term liabilities increased by \$671 million or 6%. A detailed discussion of the debt issued by the System is provided in the Debt Administration section of this discussion.

### CAPITAL ASSETS

The System's capital assets include buildings, equipment, water treatment systems and water collections systems. Such amounts are detailed as follows:

(in thousands)	2004	2003
Utility plant construction	\$ 3,564,455	2,845,080
Land	142,409	116,576
Buildings	22,071	22,071
Equipment	378,333	288,250
Water supply and wastewater treatment systems	9,619,222	9,577,106
Water distribution and sewage collection systems	7,196,035	6,676,855
Total utility plant in service	17,358,070	16,680,858
Less accumulated depreciation	5,748,397	5,362,108
Total, net utility plant in service	11,609,673	11,318,750
<b>Total capital assets</b>	<b>\$15,174,128</b>	<b>14,163,830</b>

The net increase in the System's capital assets during fiscal year 2004 was \$1.0 billion or 7.1%. Net capital asset additions for 2004 were \$1,397 million.

The 2003 capital assets have been restated. Certain amounts previously reported as utility plant construction were placed into service in prior years and should have been reclassified to utility plant in service and depreciated accordingly. In addition, certain amount included in utility plant construction should have been expenses in 2003 and in prior years.

The capital assets of the System are detailed in footnote numbers 2(d) and 4 of the notes to the financial statements.

## Management's Discussion and Analysis

**DEBT ADMINISTRATION**

The New York City Municipal Water Finance Authority, (the Authority) issues debt to pay for the capital improvements to the System. The debt program of the Authority includes commercial paper and long-term debt of the Authority and subsidized bonds issued through the New York State Environmental Facilities Corporation (EFC). The commercial paper program is the main source of financing to reimburse the City for payments made for water and sewer projects. The Authority then issues long-term debt of its own or through EFC to retire outstanding commercial paper. The Authority also issues refunding bonds to refinance higher coupon debt.

At June 30, 2004, the total outstanding debt of the system was \$14 billion, of which \$800 million was commercial paper. The remaining \$13.2 billion consisted of variable and fixed rate bonds and notes maturing in varying installments through 2039. The total outstanding long-term debt at June 30, 2004 was as follows:

(in thousands)	Issue Date
2004	\$1,712,389
2003	3,007,393
2002	2,250,595
2001	1,062,425
2000 and prior	5,200,115
<b>Total long-term debt</b>	<b>\$13,232,917</b>

In the above, bonds retired through refundings in 2004 are removed from the year in which the refunded bonds were issued.

In fiscal year 2004, the Authority issued \$1,166,160,000 of water and sewer revenue bonds directly to the public, including \$649,275,000 of refunding bonds and \$516,885,000 in long-term financing. The Authority also issued \$558,688,873 in Clean Water and Drinking Water State Revolving Fund (SRF) bonds to EFC, all of which were issued for new money purposes. The new money bond proceeds provided long-term financing of commercial paper notes which had previously financed capital improvements to New York City's water and sewer system.

Highlights of the financing program in fiscal year 2004 included continued low interest costs on both fixed and variable rate borrowing. The sizable issuance in fiscal 2004 was the result of both a sizable capital program financed by the Authority and EFC bonds and refunding opportunities, which accounted for more than one-third of the Authority's bond issuance. In fiscal 2004, the Authority continued to make

maximum use of the EFC's State Revolving Fund program, which provides an interest rate subsidy to the Authority for qualifying projects, helping to minimize the overall costs of the Authority's long term debt.

In fiscal year 2004, the Authority closed five bond transactions and entered into an interest rate exchange agreement (or swap). The First Resolution Fiscal 2004 Series A, B and C bonds consisted of bond sales directly to the public. The Second Resolution Fiscal 2004 Series 1 and Series 2 bonds were issued to EFC to secure bonds issued by EFC on behalf of the Authority.

On September 18, 2003, the Authority closed its first transaction of fiscal year 2004. The Fiscal 2004 Series A bonds were sold for a par amount of \$217 million. The issue included term bonds in years 2027 and 2035. Proceeds from the sale were used to defease all of the Authority's Series 4 and a portion of its Series 6 commercial paper notes, fund a portion of the debt service reserve fund and pay costs of issuance.

On October 9, 2003, the Authority closed its first transaction with EFC in fiscal year 2004. The Fiscal 2004 Series 1 bonds, issued to EFC in the amount of \$301,008,574 to secure bonds issued by EFC, were sold in a combined plan of finance with the Authority's Series A bonds. Proceeds were used to defease a portion of the Authority's commercial paper Series 5 and 7 notes, which had funded eligible Clean Water and Drinking Water SRF projects, and were used to pay the costs of issuance for the bonds.

On March 18, 2004, the Authority closed two transactions, Fiscal 2004 Series B and Series C, which were sold in a combined plan of finance along with Fiscal 2004 Series 2 bonds. The Series B bonds were sold for a par amount of \$347,615,000 and currently refunded Fiscal 1994 Series B, D, E, F and G bonds. The issue included serial bonds in years 2004 through 2023. Proceeds from the sale also paid for the costs of issuance.

The Fiscal 2004 Series C bonds were sold for a par amount of \$601,545,000. Proceeds from the sale were used to refund Fiscal 1996 Series A and Series B bonds and Fiscal 1997 Series A and Series B bonds, to defease all of the Authority's commercial paper Series 6 and a portion of its Series 5 Lot A notes, pay certain costs of issuance, fund a portion of the debt service reserve fund and fund a portion of the Authority's capital program. The issue included serial bonds in years 2004 through 2025 and term bonds in 2034 and 2035.

## Management's Discussion and Analysis

On April 7, 2004, the Authority closed the Fiscal 2004 Series 2 bonds, which were issued to EFC in the amount of \$257,680,299 to secure bonds issued by EFC. Proceeds were used to defease a portion of the Authority's commercial paper Series 5 and 7 notes, which had funded eligible Clean Water and Drinking Water SRF projects, and were used to pay the costs of issuance for the bonds. The issuance included serial bonds in 2004 through 2033 and term bonds in 2030 and 2033.

In fiscal 2004, the Authority defeased with revenues, \$147,450,000 of outstanding General Resolution Bonds on March 25, 2004, including portions of Fiscal 1994 Series D, 1994 Series E and 1996 Series A bonds. On June 29, 2004, \$45,716,609 of outstanding General Resolution Bonds, including portions of Fiscal 1993 Series A and 1996 Series C bonds were also defeased with revenues.

The Authority terminated its \$125 million commercial paper Series 4 notes on September 24, 2003, leaving the combined commercial paper authorized to be outstanding at \$800 million. The commercial paper program, the Authority's primary source of short-term financing, is used to reimburse the City for spending on water and sewer related projects. Throughout the year the Authority issues long-term debt to retire the outstanding commercial paper.

The total of bonds and notes payable are detailed in footnote numbers 9 and 10 of the notes to the financial statements.

### **DERIVATIVES**

On December 23, 2003, the Authority closed an interest rate exchange agreement extending to 2019 on a principal amount of \$200 million. The exchange was structured with the Authority receiving a fixed interest rate from the counterparty, in exchange for a floating rate based on the BMA Municipal Swap Index ("BMA Swap"). The fixed interest rate the Authority will receive is 3.567%, as determined by a competitive bid among six firms. The transaction effectively converts a portion of the Authority's bonds from a fixed rate basis to a floating rate basis, and increases its variable rate exposure at a cost lower than conventional variable rate demand bonds.

### **ECONOMIC FACTORS AND NEXT YEAR'S RATES**

Rates are adopted each year by the Board in May, for the following fiscal year. A rate increase of 5.5% for fiscal 2005 became effective July 1, 2004 based on projected revenues and costs.

### **REQUEST FOR INFORMATION**

This financial report is provided as an overview of the System's finances. Questions concerning any of the information in this report or requests for additional information should be directed to Raymond Orlando, Manager of Public Relations, New York City Municipal Water Finance Authority, 75 Park Place, New York, NY 10007. His phone number is (212) 788-5875 and his fax number is (212) 788-9721.

## Financial Statements

**BALANCE SHEETS**

(Year ended June 30, 2004 with summarized financial information as of June 30, 2003)

(in thousands)	New York City Water Board	New York City Municipal Water Finance Authority	Eliminations	2004 Total	2003 Total (Restated)
<b>ASSETS</b>					
Utility plant in service, less accumulated depreciation of \$5,748,397 and \$5,362,108, respectively	\$11,609,673	–	–	11,609,673	11,318,750
Utility plant construction	3,564,455	–	–	3,564,455	2,845,080
Total capital assets	15,174,128	–	–	15,174,128	14,163,830
Current assets:					
Unrestricted cash and cash equivalents	10,927	2	–	10,929	8,567
Investments	95	–	–	95	–
Accounts receivable:					
Billed, less allowance for uncollectible receivables of \$242,478 and \$268,235, respectively	298,322	–	–	298,322	336,943
Unbilled	143,625	–	–	143,625	137,500
Receivable from the City	3,323	–	–	3,323	13,213
Other	1	2,159	–	2,160	10,375
Total current unrestricted assets	456,293	2,161	–	458,454	506,598
Restricted assets:					
Cash and cash equivalents	70,407	1,067,749	–	1,138,156	1,531,401
Investments	64,810	758,132	–	822,942	738,789
Accrued interest receivable	484	3,273	–	3,757	2,358
Total current restricted assets	135,701	1,829,154	–	1,964,855	2,272,548
Total current assets	591,994	1,831,315	–	2,423,309	2,779,146
Revenue requirement to be billed by and received from the Board	–	6,861,567	(6,861,567)	–	–
Long-term deferred bond and financing expenses	–	112,540	–	112,540	111,794
Total assets	\$15,766,122	8,805,422	(6,861,567)	17,709,977	17,054,770
<b>LIABILITIES AND NET ASSETS</b>					
Long-term liabilities:					
Bonds and notes payable, less current portion	\$ –	13,028,277	–	13,028,277	12,425,832
Net discount on bonds and notes payable	–	(197,293)	–	(197,293)	(296,637)
Deferred bond refunding costs	–	(265,102)	–	(265,102)	(234,229)
Revenue requirement payable to the Authority	6,861,567	–	(6,861,567)	–	–
Total long-term liabilities	6,861,567	12,565,882	(6,861,567)	12,565,882	11,894,966
Current liabilities:					
Accounts payable and accrued expenses	6,745	30,560	–	37,305	27,102
Revenues received in advance	78,231	–	–	78,231	69,156
Current portion of bonds and notes payable	–	1,004,640	–	1,004,640	1,057,318
Payable to the City	–	451,162	–	451,162	231,390
Refunds payable to customers	18,574	–	–	18,574	20,373
Total current liabilities	103,550	1,486,362	–	1,589,912	1,405,339
Total liabilities	6,965,117	14,052,244	(6,861,567)	14,155,794	13,300,305
Net Assets:					
Invested in capital assets, net of related debt	15,174,128	(11,805,773)	–	3,368,355	3,271,440
Restricted for debt service	–	179,106	–	179,106	203,695
Restricted for operations and maintenance	135,701	–	–	135,701	132,107
Unrestricted (deficit)	(6,508,824)	6,379,845	–	(128,979)	147,223
Total net assets	8,801,005	(5,246,822)	–	3,554,183	3,754,465
Total liabilities and net assets	\$15,766,122	8,805,422	(6,861,567)	17,709,977	17,054,770

See accompanying notes to the financial statements.

## Financial Statements

**STATEMENTS OF REVENUE, EXPENSES AND CHANGES IN NET ASSETS**

(Year ended June 30, 2004 with summarized financial information for the year ended June 30, 2003)

(in thousands)	New York City Water Board	New York City Municipal Water Finance Authority	2004 Total	2003 Total (Restated)
Operating revenues:				
Water supply and distribution	\$ 713,097	–	713,097	690,093
Sewer collection and treatment	984,753	–	984,753	952,985
Other operating revenues	75,283	–	75,283	68,842
Total operating revenues	<u>1,773,133</u>	<u>–</u>	<u>1,773,133</u>	<u>1,711,920</u>
Operating expenses:				
Operations and maintenance	933,736	–	933,736	875,762
Bad debt expense	116,108	–	116,108	89,400
Administration and general	4,970	14,883	19,853	15,181
Total operating expenses	<u>1,054,814</u>	<u>14,883</u>	<u>1,069,697</u>	<u>980,343</u>
Depreciation and amortization	409,139	42,446	451,585	389,626
Operating income (loss)	<u>309,180</u>	<u>(57,329)</u>	<u>251,851</u>	<u>341,951</u>
Nonoperating revenue (expense):				
Interest expense	–	(612,054)	(612,054)	(584,347)
Loss on retirement of fixed assets	(25,214)	–	(25,214)	–
Subsidy income	–	68,311	68,311	65,816
Investment income	1,237	85,712	86,949	96,236
Net income (loss) before capital contributions	<u>285,203</u>	<u>(515,360)</u>	<u>(230,157)</u>	<u>(80,344)</u>
Capital contributions	29,875	–	29,875	7,233
Change in net assets	<u>315,078</u>	<u>(515,360)</u>	<u>(200,282)</u>	<u>(73,111)</u>
Net assets (deficit) at beginning of year, as restated	8,485,927	(4,731,462)	3,754,465	3,827,576
Net assets (deficit) at end of year	<u>\$8,801,005</u>	<u>(5,246,822)</u>	<u>3,554,183</u>	<u>3,754,465</u>

See accompanying notes to the financial statements.



## Financial Statements

**STATEMENTS OF CASH FLOW**

(Year ended June 30, 2004 with summarized financial information for the year ended June 30, 2003)

(in thousands)	New York City Water Board	New York City Municipal Water Finance Authority	2004 Total	2003 Total (Restated)
<b>Cash flows from operating activities:</b>				
Receipts from customers	\$ 1,696,738	—	1,696,738	1,588,898
Payments for operations and maintenance	(874,854)	—	(874,854)	(868,811)
Payments for administration	(4,732)	(14,948)	(19,680)	(14,616)
Net cash provided by (used in) operating activities	817,152	(14,948)	802,204	705,471
<b>Cash flows from capital and related financing activities:</b>				
Proceeds from issuing bonds, notes and other borrowings, net of issuance costs	—	2,728,279	2,728,279	4,679,212
Acquisition and construction of capital assets	—	(1,238,298)	(1,238,298)	(1,217,895)
Payments by the Board to the Authority	(811,421)	811,421	—	—
Repayments of bonds, notes and other borrowings	—	(2,174,239)	(2,174,239)	(3,343,065)
Interest paid on bonds, notes and other borrowings	—	(515,787)	(515,787)	(576,516)
Net cash used in capital and related financing activities	(811,421)	(388,624)	(1,200,045)	(458,264)
<b>Cash flows from investing activities:</b>				
Proceeds from sales and maturities of investments	64,422	89,473	153,895	61,240
Purchases of investments	(64,845)	(175,659)	(240,504)	(114,299)
Interest on investments	1,142	92,425	93,567	163,167
Net cash provided by investing activities	719	6,239	6,958	110,108
Net increase (decrease) in cash and cash equivalents	6,450	(397,333)	(390,883)	357,315
Cash and cash equivalents, beginning of year	74,884	1,465,084	1,539,968	1,182,653
Cash and cash equivalents, end of year	\$ 81,334	1,067,751	1,149,085	1,539,968

Cash and cash equivalents are reported in the Balance Sheet as follows:

Unrestricted cash and cash equivalents	\$ 10,927	2	10,929	8,567
Restricted cash and cash equivalents	70,407	1,067,749	1,138,156	1,531,401
	\$ 81,334	1,067,751	1,149,085	1,539,968

Reconciliation of Operating Income to Net Cash Provided by (used in) Operating Activities:

Operating income (Loss)	\$ 309,180	(57,329)	251,851	341,951
Adjustments to reconcile operating income to net cash provided by (used in) operating activities:				
Depreciation and amortization	409,139	42,446	451,585	389,626
Bad debt expense	116,108	—	116,108	89,400
Operations and maintenance expense paid with bond proceeds	43,230	—	43,230	25,941
Changes in net assets and liabilities:				
Receivables, net	(83,609)	—	(83,609)	(119,893)
Receivable from the City	9,890	—	9,890	(22,216)
Accounts payable	5,938	(65)	5,873	565
Revenues received in advance	9,075	—	9,075	(6,875)
Refunds payable	(1,799)	—	(1,799)	6,972
Net cash provided by (used in) operating activities	\$ 817,152	(14,948)	802,204	705,471

The following are the noncash capital and related financing activities:

- Interest expense includes the amortization of premium and discount in the amount of \$8,189 in 2004 and \$7,312 in 2003
- Capital expenditures in the amount of \$451,162 and \$231,390 had been incurred but not paid at June 30, 2004 and June 30, 2003
- The Board received capital assets of \$29,878 and \$7,233 in 2004 and 2003, respectively, which represents capital contributed by the City

See accompanying notes to the financial statements.

Notes to Financial Statements, June 30, 2003 and 2004

(with summarized financial information for the year ended June 30, 2003)

**1 ORGANIZATION**

The New York City Water and Sewer System (the “System”) provides water supply and distribution, and sewage collection, treatment, and disposal for The City of New York (the “City”). The System, as presented in the accompanying financial statements, began operations on July 1, 1985 and is a joint operation consisting of two legally separate and independent entities, the New York City Municipal Water Finance Authority (the “Authority”) and the New York City Water Board (the “Board”). The Authority is a public benefit corporation created in accordance with the New York City Municipal Water Finance Act (the “Act”), duly enacted into law as Chapter 513 of the laws of 1984 of the State of New York, as amended by Chapter 514 of the laws of 1984 of the State of New York. The Board was created by Chapter 515 of the laws of 1984 of the State of New York. The Act empowers the Authority to issue bonds or notes to finance the cost of capital improvements to the System, and to refund any and all outstanding bonds and general obligation bonds of the City issued for water and sewer purposes. The Act empowers the Board to lease the System from the City and to fix and collect rates, fees, rents and other charges for the use of, or for services furnished, rendered, or made available by the System, to produce cash sufficient to pay debt service on the Authority’s bonds and to place the System on a self-sustaining basis.

The physical operation and capital improvements of the System are performed by the City’s Department of Environmental Protection subject to contractual agreements with the Authority and Board.

In accordance with Statement 14 of Governmental Accounting Standards Board (GASB), the Board and the Authority are considered to be part of the same reporting entity (the System) since they are fiscally interdependent. Accordingly, the accompanying financial statements for the System present the individual financial statements of the Board and the Authority as major funds. In addition, the accompanying financial statements present a total column which represents the entity wide financial statements of the System. Transactions and balances between the Board and the Authority are eliminated in the entity wide financial statements.

**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The accompanying financial statements of the System have been prepared on the accrual basis of accounting. Revenues are recognized when earned and expenses recognized when incurred. GASB Statement No. 20, Accounting and Financial Reporting for Proprietary Funds and Other Government Entities that Use Proprietary Funds, provides proprietary activities with a choice of authoritative guidance issued after November 30, 1989. The System has elected to follow GASB pronouncements exclusively after that date. Other significant accounting policies are:

**(a) Investments and Cash Equivalents**

Investments and cash equivalents consist principally of securities of the United States and its agencies, certificates of deposit, and repurchase agreements with maturity periods of one year or less, and are carried at amortized cost, which approximates fair value. For purposes of the statements of cash flows, the System generally considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents.

**(b) Restricted Assets**

Proceeds from the issuance of debt and monies set aside for the operation and maintenance of the System are classified as restricted by applicable bond indentures.

**(c) Bond Discount and Bond Issuance Costs**

Bond discount and bond issuance costs are amortized over the life of the related bond issue, using the effective yield method of amortization for bond discount and the straight-line method for bond issuance costs.

**(d) Utility Plant**

Utility plant acquired through purchase or internal construction is recorded at cost, net of retirements. Contributed utility plant is recorded at its estimated historical cost based on appraisals or other methods when historical cost information is not available, net of depreciation. Depreciation is computed using the straight-line method based upon estimated useful lives, as follows:

	Years
Buildings	40-50
Water supply and wastewater treatment systems	15-50
Water distribution and sewage collection systems	15-75
Equipment	5-35

## Notes to Financial Statements, June 30, 2003 and 2004

(with summarized financial information for the year ended June 30, 2003)

Maintenance and repairs of property are charged to maintenance expense. Replacements and betterments are recorded as utility plant.

**(e) Operating Revenues and Operating Expenses**

Operating revenues consist of customer payments for services of the System. Revenues are based on billing rates imposed by the Board and upon customers' water and sewer usage. The System records estimated unbilled revenue at year end.

Operating expenses consist of administration, maintenance, repair and operations of the System, administration costs of the Board and the Authority, rental payments to the City, and bad debt expense.

**(f) Deferred Revenues**

Revenues received in advance of the period to which they relate are deferred and recorded as revenue when earned.

**(g) Deferred Bond Refunding Costs**

Deferred bond refunding costs represent the accounting loss incurred in advance refundings of outstanding bonds. In accordance with the provisions of GASB Statement No. 23, Accounting and Financial Reporting of Debt Reported by Proprietary Activities, gains or losses arising from debt refundings are deferred and amortized over the lesser of the remaining life of the old debt or the life of the new debt.

**(h) Comparative Summary Prior Year Information and Reclassifications**

Selected comparative information for 2003 has been provided in the accompanying financial statements and footnotes. Such information does not include all information required for

presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the System's financial statements for the year ended June 30, 2003 from which it has been derived. Certain 2003 amounts have been reclassified to conform to the 2004 financial statement presentation.

**(i) Use of Estimates**

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions in determining the amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual amounts could differ from those estimates.

**3 FINANCING AGREEMENT**

The Financing Agreement (the "Agreement") provides that the Authority will issue bonds to finance the cost of capital investment in the water and sewer system serving the City. It also sets forth the funding priority for the debt service costs of the Authority, operating costs of the water and sewer system, and the rental payment to the City.

**4 UTILITY PLANT**

As discussed in footnote 14, the System has restated its 2003 financial statements to adjust capital assets. The following is a summary of utility plant activity for the fiscal years ended June 30, 2004 and 2003.

(in thousands)	Balance at June 30, 2002 (as restated)	Additions	Deletions	Balance at June 30, 2003 (as restated)	Additions	Deletions	Balance at June 30, 2004
Utility construction	\$ 2,446,417	1,146,968	748,305	2,845,080	1,444,655	725,280	3,564,455
Land	89,891	26,685	—	116,576	25,833	—	142,409
Buildings	21,615	456	—	22,071	—	—	22,071
Equipment	275,701	12,549	—	288,250	107,364	17,281	378,333
Water supply and wastewater treatment systems	9,123,546	453,560	—	9,577,106	72,903	30,787	9,619,222
Water distribution and sewage collection systems	6,443,819	281,740	48,704	6,676,855	519,180	—	7,196,035
Total	18,400,989	1,921,958	797,009	19,525,938	2,169,935	773,348	20,922,525
Less accumulated depreciation	5,065,891	344,921	48,704	5,362,108	409,141	22,852	5,748,397
Total	\$13,335,098	1,577,037	748,305	14,163,830	1,760,794	750,496	15,174,128

## Notes to Financial Statements, June 30, 2003 and 2004

(with summarized financial information for the year ended June 30, 2003)

**5 NET ASSETS**

At June 30, 2004 and 2003, the Authority had a net asset deficit of \$5,247 million and \$4,731 million, respectively, which amount is less than the \$8,801 million and \$8,486 million total net assets of the Board at June 30, 2004 and 2003, respectively.

**6 INVESTMENTS, CASH EQUIVALENTS AND DEPOSITS CASH**

The Water and Sewer General Revenue Bond Resolution (the "Resolution") authorizes the investment of bond proceeds. The guidelines issued by the Office of the New York State Comptroller and the Resolution establish the criteria for permissible investments of the System. In addition, the Board and the Authority have investment guidelines approved by their respective Boards of Directors. The System may invest in obligations of the Federal government or any subdivision or instrumentality thereof, obligations of the State of New York or any subdivision or instrumentality thereof provided that they are in the two highest rating categories of a rating agency, bankers' acceptances or certificates of deposit (CDs) issued by a New York State commercial bank with capital or surplus in excess of \$100 million, corporate securities or commercial paper rated highest by a rating agency when compared to similar type securities, or repurchase agreements that are collateralized by obligations of the Federal government.

Investments and deposits held by the System at June 30, 2004, and 2003 comprised:

(in thousands)	2004	2003
Unrestricted Investments	\$ 95	-
Unrestricted cash, cash equivalents (including accrued interest)	\$10,929	8,567
Restricted cash, cash equivalents and investments (including accrued interest)	1,964,855	2,272,548
	<u>\$1,975,879</u>	<u>2,281,115</u>

This amount is comprised of:

Carrying amount of deposits (including CDs)	\$ 11,028	7,146
Investments (including accrued interest)	1,964,851	2,273,969
	<u>\$1,975,879</u>	<u>2,281,115</u>

**Cash Deposits**

The System follows the New York City Banking Commission designations for the System's bank depositories. The Commission consists of the Comptroller, the Mayor, and the Finance Commissioner of the City and uses independent bank rating agencies in part to assess the financial soundness of each bank, and the banking relationships are under constant operational and credit reviews. Each bank in which the System's cash is deposited is required to have its principal office in New York State and have capital stock, surplus, and undivided earnings aggregating at least \$100 million. The System had \$200 thousand on deposit at June 30, 2004 and 2003, which were covered by Federal depository insurance and the balance was uncollateralized.

**Investments**

The System's investment of cash is limited to U.S. Government guaranteed securities and U.S. Government agency securities purchased directly and through repurchase agreements as well as New York State securities, mutual funds and guaranteed investment contracts. The repurchase agreements must be collateralized by U.S. Government guaranteed securities in a range of 100% to 300% for the Board and 102% for the Authority. The fair value of investments is determined based on quoted market prices. All investments are held in the Authority's name by the trustee or in the Board's name by the agent.

Notes to Financial Statements, June 30, 2003 and 2004

(with summarized financial information for the year ended June 30, 2003)

As of June 30, 2004 the System had the following investments and maturities:

Investment Type (in thousands)	Amortized Cost	Fair Value	Investment Maturity
<b>Unrestricted</b>			
Certificate of Deposit	\$ 95	96	Greater than one year
<b>Restricted</b>			
US Government securities	\$1,233,127	1,233,668	Less than one year
New York State securities	42,916	44,391	Greater than one year
Repurchase agreements	19,780	19,797	Less than one year
Guaranteed investment contracts	665,176	666,899	Greater than one year
	<u>\$1,960,999</u>	<u>1,964,755</u>	

As of June 30, 2003 the System had the following investments and maturities:

Investment Type (in thousands)	Amortized Cost	Fair Value	Investment Maturity
<b>Unrestricted</b>			
Mutual Funds	\$ 1,005	1,005	Less than one year
Repurchase agreements	850	850	Less than one year
	<u>\$ 1,855</u>	<u>1,855</u>	
<b>Restricted</b>			
US Government securities	\$1,577,965	1,578,479	Less than one year
New York State securities	5,756	5,901	Greater than one year
Repurchase agreements	67,000	67,099	Less than one year
Guaranteed investment contracts	619,084	620,685	Less than one year
	<u>\$2,269,805</u>	<u>2,272,164</u>	

## Notes to Financial Statements, June 30, 2003 and 2004

(with summarized financial information for the year ended June 30, 2003)

**7 LEASE AGREEMENT**

The Board is party to a long-term lease (the "Lease") with the City, which transfers all the water and sewer related real and personal property to the Board for the term of the lease. The Lease term commenced on July 1, 1985, and continues until the later of the fortieth anniversary of the commencement of the lease, or the date on which all bonds, notes or other obligations of the Authority are paid in full, or provisions for such payment have been made pursuant to the applicable debt instrument. The Lease provides for payments to the City to cover the following:

(a) an amount sufficient to pay the cost of administration, maintenance, repair and operation of the leased property, which includes overhead costs incurred by the City attributable to the leased property, net of the amount of any Federal, State, or other operating grants received by the City;

(b) an amount sufficient to reimburse the City for capital costs incurred by the City for the construction of capital improvements to the leased property which are not paid or reimbursed from any other source.

In addition to the payments described above, the Board pays rent to the City in each fiscal year in an amount not to exceed the greater of (a) the principal and interest payable on general obligation bonds issued by the City for water and sewer purposes certified by the City to be paid within such

fiscal year or (b) 15% of principal and interest payable on the bonds of the Authority to be paid within such fiscal year.

A summary of operation and maintenance expenses for the years ended June 30, 2004 and 2003 is as follows:

(in thousands)	2004	2003
Water transmission and distribution	\$ 284,461	285,929
Sewer collection systems	338,566	336,391
City agency support cost	52,399	36,557
Fringe benefits	70,466	73,740
Payments for watershed improvements	43,292	25,942
Judgments and claims	27,910	15,055
	817,094	773,614
Rental payments to the City	116,642	102,148
	<u>\$ 933,736</u>	<u>875,762</u>

**8 PAYABLE TO AND RECEIVABLE FROM THE CITY**

As of June 30, 2004 and 2003, all utility construction recorded by the System, which has not been reimbursed to the City, has been recorded as a payable to the City, net of the amount of any State or Federal capital grants received by the City.

As of June 30, 2004 and 2003 the System had a receivable from the City for overpayment of operations and maintenance expense.

**9 SHORT-TERM LIABILITIES**

In fiscal years 2003 and 2004 the changes in short-term liabilities were as follows:

(in thousands)	Balance at June 30, 2002	Additions	Deletions	Balance at June 30, 2003	Additions	Deletions	Balance at June 30, 2004
Commercial paper <sup>1</sup>	\$628,000	1,558,800	1,361,800	825,000	964,500	989,500	800,000

<sup>1</sup>Commercial paper is used to pay construction costs in advance of long term bond financing.

## Notes to Financial Statements, June 30, 2003 and 2004

(with summarized financial information for the year ended June 30, 2003)

Commercial paper activity comprises the following for the year ended June 30, 2004:

(in thousands)	Balance at June 30, 2003	Issued	Retired	Balance at June 30, 2004
Commercial Paper Series 1 —				
Variable Rate, Short-term Rolling Maturity Backed by Letter of Credit	\$ 200,000	—	—	200,000
Commercial Paper Series 4 —				
Variable Rate, Short-term Rolling Maturity Backed by Letter of Credit	125,000	—	125,000	—
Commercial Paper Series 5 —				
Variable Rate, Short-term Rolling Maturity Backed by Line of Credit	200,000	203,300	203,300	200,000
Commercial Paper Series 6 —				
Variable Rate, Short-term Rolling Maturity Backed by Line of Credit	200,000	275,000	275,000	200,000
Commercial Paper Series 7 —				
Variable Rate, Short-term Rolling Maturity	100,000	486,200	386,200	200,000
Total commercial paper payable	<u>\$ 825,000</u>	<u>964,500</u>	<u>989,500</u>	<u>800,000</u>

## 10 LONG-TERM LIABILITIES

In fiscal years 2003 and 2004, the changes in long-term liabilities were as follows:

Bonds payable: (in thousands)	Balance at June 30, 2002	Additions	Deletions	Balance at June 30, 2003	Additions	Deletions	Balance at June 30, 2004	Due Within One Year
First resolution	\$ 8,856,014	2,010,310	1,232,234	9,634,090	1,166,160	1,057,437	9,742,813	94,127
Second resolution	2,662,990	1,110,102	749,031	3,024,061	558,688	92,645	3,490,104	110,513
Total bonds payable	11,519,004	3,120,412	1,981,265	12,658,151	1,724,848	1,150,082	13,232,917	204,640
Less discounts (net)	371,892	(49,341)	25,914	296,637	(58,916)	40,428	197,293	—
Less deferred refunding costs	208,521	50,889	25,181	234,229	53,534	22,661	265,102	—
Total long-term liabilities	<u>\$10,938,591</u>	<u>3,118,864</u>	<u>1,930,170</u>	<u>12,127,285</u>	<u>1,730,230</u>	<u>1,086,993</u>	<u>12,770,522</u>	

## Notes to Financial Statements, June 30, 2003 and 2004

(with summarized financial information for the year ended June 30, 2003)

With respect to all series, the Board has agreed to maintain rates and charges to provide revenues at levels sufficient to pay principal and interest requirements as well as to meet certain debt service coverage and operating cost funding requirements. All series are specific obligations of the Authority payable solely from and secured by a pledge of and lien on the gross revenue of the System, as defined.

Certain bonds issued by the Authority involve the concurrent issuance of long-term variable rate securities that are matched with long-term floating rate securities. These obligations, taken together as a whole, yield a fixed rate of interest at all times. These securities have been issued to achieve a lower prevailing fixed rate of interest in relation to traditional fixed rate bonds.

During 2004 and 2003, the Authority issued \$949.1 million and \$1.0 billion, respectively, of bonds to advance refund \$652 million and \$973.5 million, respectively, of outstanding bonds. The advance refundings resulted in an accounting loss of \$21.2 million and \$50.9 million, respectively. The Authority in effect reduced its aggregate debt service by \$102 million and \$123 million, respectively, and obtained an economic benefit of \$69.4 million and \$102 million, respectively.

During 2004 and 2003, the Authority defeased \$213.3 million and \$145.1 million, respectively, of outstanding bonds with \$215.1 million and \$158.1 million, respectively, of current revenue which resulted in an accounting loss of

\$16.5 million and \$15.7 million, respectively.

During 2003 the Authority renegotiated the terms of \$666.6 million of its notes with the New York State Environmental Facilities Corporation. The Authority in effect increased its aggregate debt service by \$173.7 million and obtained an economic benefit of \$52.3 million.

During 2004 the Authority issued \$50 million of bonds that will refund \$50 million of principal of the 2003 B issue in June 2005. During 2003 the Authority issued \$50 million of bonds that refunded \$50 million of the 2003 B issue in June 2004.

The Authority has defeased cumulatively \$6.664 billion and \$5.759 billion of outstanding bonds as of June 30, 2004 and 2003, respectively, by placing proceeds of refunding bonds issued in an irrevocable escrow account to provide for all future debt service payments on defeased bonds. Proceeds were used to purchase U.S. Government securities that were placed in the irrevocable escrow account. Accordingly, the escrow account assets and liabilities for the defeased bonds are not included in the Authority's financial statements.

As of June 30, 2004 and 2003, \$5.493 billion and \$4.663 billion of the defeased bonds respectively had been retired from the assets of the escrow accounts.

Debt service requirements to maturity including amounts relating to commercial paper at June 30, 2004 are as follows:

Year ending June 30 (in thousands)	Principal	Interest <sup>1</sup>	Total
2005	\$ 1,004,640	500,565	1,505,205
2006	221,605	487,295	708,900
2007	174,735	497,594	672,329
2008	208,936	500,908	709,844
2009	235,382	496,057	731,439
2010-2014	1,447,627	2,370,636	3,818,263
2015-2019	1,990,228	2,079,480	4,069,708
2020-2024	2,349,929	1,694,362	4,044,291
2025-2029	2,875,320	1,197,834	4,073,154
2030-2034	2,861,255	515,670	3,376,925
2035-2039	663,260	39,932	703,192
Total	\$14,032,917	10,380,333	24,413,250

<sup>1</sup>Includes interest for variable rate bonds estimated at .92% which is the rate at the end of the fiscal year. Variable rate bonds are sold daily or weekly and interest rates are determined by the market on the day sold.



## Notes to Financial Statements, June 30, 2003 and 2004

(with summarized financial information for the year ended June 30, 2003)

Bonds, notes payable, and commercial paper comprise the following for the year ended June 30, 2004:

(in thousands)	Balance at June 30, 2003	Issued	Retired	Balance at June 30, 2004
1991 Fiscal Series B — 6.00% to 7.25% Serial and Term Bonds maturing in varying installments through 2012	\$ 19,250	—	3,165	16,085
1992 Fiscal Series B — 6.66% to 6.86% Serial and Term Bonds maturing in varying installments through 2014	21,610	—	3,927	17,683
1993 Fiscal Series A — 5.875% to 6.0% Serial, Term, and Capital Appreciation Bonds maturing in varying installments through 2013	229,380	—	63,515	165,865
1993 Fiscal Series C — Adjustable Rate Term Bonds maturing 2022	100,000	—	—	100,000
1994 Fiscal Series 1 — 3.00% to 6.00% Serial Bonds maturing in varying installments through 2013	31,805	—	—	31,805
1994 Fiscal Series B — 4.875% to 5.125% Fixed Rate Bonds maturing in varying installments through 2019	285,940	—	285,940	—
1994 Fiscal Series C — Adjustable Rate term bonds maturing in 2023	200,000	—	—	200,000
1994 Fiscal Series D — Auction Rate Bonds maturing in varying installments through 2013	83,500	—	83,500	—
1994 Fiscal Series E — Inverse Rate Bonds maturing in varying installments through 2013	83,500	—	83,500	—
1994 Fiscal Series F — 5.40% to 5.75% Serial Bonds maturing in varying installments through 2023	117,900	—	117,900	—
1994 Fiscal Series G — Adjustable, Auction and Leveraged Reverse Rate Bonds maturing in varying installments through 2024	205,000	—	20,000	185,000
1995 Fiscal Series A — Adjustable Rate Term Bonds maturing in varying installments through 2025	216,700	—	—	216,700
1995 Fiscal Series 1 — 5.25% to 6.875% Serial Bonds maturing in varying installments through 2016	36,602	—	5,387	31,215
1996 Fiscal Series A — 5.10% to 5.15% Serial Bonds maturing in varying installments through 2023	122,150	—	122,150	—
1996 Fiscal Series B — 5.75% to 5.875% Serial Bonds maturing in varying installments through 2026	491,025	—	114,415	376,610
1996 Fiscal Series C — 4.90% to 5.75% Serial Bonds maturing in varying installments through 2017	76,645	—	14,525	62,120
1997 Fiscal Series A — 4.85% to 6.0% Serial Bonds maturing in varying installments through 2026	365,125	—	23,735	341,390
1997 Fiscal Series B — 5.75% to 5.80% Serial Bonds maturing in varying installments through 2029	700,000	—	43,460	656,540
1998 Fiscal Series 1 — 4.00% to 5.35% Serial Bonds maturing in varying installments through 2017	36,105	—	1,795	34,310
1998 Fiscal Series 3 — 4.30% to 6.00% Serial Bonds maturing in varying installments through 2016	405,580	—	25,546	380,034

## Notes to Financial Statements, June 30, 2003 and 2004

(with summarized financial information for the year ended June 30, 2003)

(in thousands)	Balance at June 30, 2003	Issued	Retired	Balance at June 30, 2004
1998 Fiscal Series 4 — 3.60% to 5.20% Serial Bonds maturing in varying installments through 2018	\$ 12,525	—	700	11,825
1998 Fiscal Series 6 — 4.827% to 5.125% Serial Bonds maturing in varying installments through 2019	15,965	—	744	15,221
1998 Fiscal Series A — 4.80% to 5.125% Serial Bonds maturing in varying installments through 2022	283,850	—	—	283,850
1998 Fiscal Series B — 5.125% to 5.25% Serial Bonds maturing in varying installments through 2030	449,525	—	—	449,525
1998 Fiscal Series C — 4.30% to 5.125% Serial Bonds maturing in varying installments through 2021	87,050	—	285	86,765
1998 Fiscal Series D — 4.25% to 5.00% Serial and Capital Appreciation Bonds maturing in varying installments through 2025	384,400	—	3,525	380,875
1999 Fiscal Series 2 — 4.00% to 5.25% Serial Bonds maturing in varying installments through 2020	108,016	—	4,286	103,730
1999 Fiscal Series A — 4.75% to 5.00% Serial Bonds maturing in varying installments through 2031	301,470	—	—	301,470
1999 Fiscal Series B — 4.0% to 5.25% Serial, Term and Capital Appreciation Bonds maturing in varying installments through 2020	232,805	—	6,975	225,830
2000 Fiscal Series A — 5.50% to 5.75% Serial Bonds maturing in varying installments through 2032	275,735	—	—	275,735
2000 Fiscal Series B — 6.00% to 6.10% Serial Bonds maturing in varying installments through 2033	131,865	—	—	131,865
2000 Fiscal Series C — Adjustable Rate Term Bonds maturing in 2033	107,500	—	—	107,500
2000 Fiscal Series 2 — 3.80% to 5.96% Serial Bonds maturing in varying installments through 2019	11,025	—	460	10,565
2001 Fiscal Series A — 5.50% Term Bonds maturing in varying installments through 2033	328,225	—	—	328,225
2001 Fiscal Series B — 4.5% to 5.125% Serial and Term Bonds maturing in varying installments through 2031	68,400	—	145	68,255
2001 Fiscal Series C — 5.125% Term Bonds maturing in varying installments through 2033	112,040	—	—	112,040
2001 Fiscal Series D — 4.5% to 5.5% Serial and Capital Appreciation Bonds maturing in varying installments through 2025	288,375	—	4,705	283,670
2001 Fiscal Series E — 4.5% to 5.25% Serial and Term Bonds maturing in varying installments through 2031	86,105	—	—	86,105
2001 Fiscal Series F — Adjustable Rate Bonds maturing in varying installments through 2033	184,130	—	—	184,130
2002 Fiscal Series A — 5.00% to 5.75% Serial and Term Bonds maturing in varying installments through 2033	216,305	—	—	216,305
2002 Fiscal Series B — 3.625% to 5.00% Serial and Term Bonds maturing in varying installments through 2026	171,455	—	—	171,455
2002 Fiscal Series C — 4.1% to 5.125% Serial and Term Bonds maturing in varying installments through 2032	46,580	—	—	46,580
2002 Fiscal Series D — 3.0% to 4.90% Serial and Term Bonds maturing in varying installments through 2020	41,745	—	—	41,745
2002 Fiscal Series E — 3.4% to 5.0% Serial and Term Bonds maturing in varying installments through 2026	213,850	—	—	213,850

## Notes to Financial Statements, June 30, 2003 and 2004

(with summarized financial information for the year ended June 30, 2003)

(in thousands)	Balance at June 30, 2003	Issued	Retired	Balance at June 30, 2004
2002 Fiscal Series F — 3.6% to 5.0% Serial and Term Bonds maturing in varying installments through 2029	\$ 105,635	—	—	105,635
2002 Fiscal Series G — 5.00% to 5.125% Term Bonds maturing in varying installments through 2034	216,375	—	—	216,375
2002 Fiscal Series 1 — 4.82% to 5.25% Serial Bonds maturing in varying installments through 2031	196,816	—	5,091	191,725
2002 Fiscal Series 2 — 4.22% to 5.00% Serial Bonds maturing in varying installments through 2031	68,928	—	2,251	66,677
2002 Fiscal Series 3 — 4.65% to 5.00% Serial Bonds maturing in varying installments through 2031	501,513	—	10,812	490,701
2002 Fiscal Series 4 — 5.13% to 6.74% Serial Bonds maturing in varying installments through 2023	223,498	—	7,480	216,018
2002 Fiscal Series 5 — 3.82% to 5.21% Serial Bonds maturing in varying installments through 2031	177,416	—	3,584	173,832
2002 Fiscal Series 6 — 3.82% to 5.21% Serial Bonds maturing in varying installments through 2019	94,769	—	4,327	90,442
2002 Fiscal Series 7 — 7.4% to 7.5% Serial Bonds maturing in varying installments through 2012	11,050	—	1,795	9,255
2003 Fiscal Series A — 4.0% to 6.0% Serial, Term and muni CPI Bonds maturing in varying installments through 2034	719,180	—	—	719,180
2003 Fiscal Series B — 4.0% to 5.25% Refundable Principal Installment Bonds maturing in varying installments through 2006	150,000	—	50,000	100,000
2003 Fiscal Series C — Adjustable Rate Bonds maturing in 2018	300,300	—	—	300,300
2003 Fiscal Series D — 2.0% to 5.25% Serial and Term Bonds maturing in varying installments through 2017	244,545	—	1,720	242,825
2003 Fiscal Series E — 5% Term Bonds maturing in 2034 and 2038	367,265	—	—	367,265
2003 Fiscal Series F — Adjustable Rate Bonds maturing in 2035	201,655	—	—	201,655
2003 Fiscal Series 1 — 4.23% to 4.375% Serial Bonds maturing in varying installments through 2032	147,258	—	2,029	145,229
2003 Fiscal Series 2 — 5.27% Serial Bonds maturing in varying installments through 2028	593,638	—	10,252	583,386
2003 Fiscal Series 3 — 5.15% Serial Bonds maturing in varying installments through 2025	21,755	—	620	21,135
2003 Fiscal Series 4 — 5.18% Serial Bonds maturing in varying installments through 2025	34,640	—	990	33,650
2003 Fiscal Series 5 — 4.23% to 4.45% Serial Bonds maturing in varying installments through 2032	295,157	—	2,388	292,769
2004 Fiscal Series A — 5.0% Term Bonds maturing in 2027 and 2035	—	217,000	—	217,000
2004 Fiscal Series B — 2.00% to 5.00% Serial and Term Bonds maturing in varying installments through 2023	—	347,615	5,665	341,950
2004 Fiscal Series C — 2.00% to 5.00% Serial and Term Bonds maturing in Varying installments through 2035	—	601,545	4,685	596,860
2004 Fiscal Series 1 — 4.12% to 4.45% Serial Bonds maturing in 2033	—	301,008	1,829	299,179
2004 Fiscal Series 2 — 4.46% Serial Bonds maturing in 2026	—	257,680	280	257,400
Total debt payable	12,658,151	1,724,848	1,150,083	13,232,917
Current portion of bonds and notes payable	232,319	217,099	244,778	204,640
Bonds and notes payable, less current portion	\$12,425,832	1,507,749	905,305	13,028,277

## Notes to Financial Statements, June 30, 2003 and 2004

(with summarized financial information for the year ended June 30, 2003)

**Derivatives**

In 2004, the Authority entered into a \$200 million interest rate exchange agreement under which the Authority receives a fixed rate in exchange for a floating rate based on the BMA Municipal Swap Index. This effectively converted a portion of the Authority's second resolution bonds issued through EFC to variable rate bonds. The terms of this agreement require the Authority to pay the BMA index and the counterparty to pay 3.567%.

In 2003, the Authority sold \$20 million of muni-CPI bonds in the 2013 maturity of its Fiscal 2003 Series A issue. In connection with the muni-CPI bonds the Authority entered into an interest rate exchange agreement under which the Authority receives a floating rate tied to the consumer price index, which matches the rate on the bonds, and pays a fixed interest rate. This allowed the Authority to achieve a yield 10 basis points lower than traditional fixed rate debt with a 2013 maturity. The terms of this transaction require the counterparty to pay the Authority the muni-CPI rate, which is set at 1.53% plus a floating rate CPI, with the CPI being equal to the change in the consumer price index for a given period.

In keeping with market standards, the Authority or the counterparty may terminate the swap agreements if the other party fails to perform under its terms as defined in the agreements. The Authority views termination risk to be remote at this time. Depending on the fair value at the time of termination, the Authority may have a liability to the counterparties.

Through the swap agreement the Authority is exposed to credit risk i.e., the risk that the counterparties fails to perform its contractual obligations. The appropriate measurement of this risk at the reporting date is the fair value of the swap. The fair value of the swaps at June 30, 2004 and June 30, 2003 respectively, was approximately \$3 and \$1 million, respectively, in favor of the counterparty. To mitigate credit risk, the agreement requires the counterparty to post collateral for the Authority's benefit if it is downgraded below a designated threshold, as defined in the agreement.

**11 RESTRICTED ASSETS**

Certain cash and investments, plus accrued interest and other receivables, of the System are restricted as follows:

(In thousands)	2004	2003
<b>The Board</b>		
Operation and maintenance reserve account	\$ 135,691	132,097
Operation and maintenance reserve general account	10	10
	<u>135,701</u>	<u>132,107</u>
<b>The Authority</b>		
Revenue fund	179,106	203,695
Debt service reserve fund	698,518	678,115
Construction fund	289,540	556,314
Escrow fund	661,990	702,317
	<u>1,829,154</u>	<u>2,140,441</u>
	<u>\$1,964,855</u>	<u>2,272,548</u>

The operation and maintenance reserve account is established as a depository to hold the operations and maintenance reserve fund as required by the Resolution. It is required to hold one-sixth of the operating expenses as set forth in the annual budget. It is funded through the cash receipts of the Board. The operation and maintenance reserve general account is established as a depository to hold all excess funds of the Board after all legally mandated transfers have been made. It is available to meet any deficiencies in the flow of funds including debt service and alternatively can be used as a financing source for capital expenditures.

The revenue fund is established as a depository to fund the debt service, Authority expense, debt service reserve and escrow funds. It is funded through cash transfers from the Board. The debt service reserve fund is established as a depository to hold the maximum annual debt service requirement for the next current or any future fiscal year. It is funded through revenue bond proceeds and the revenue fund. The debt service fund is established as a depository to pay all principal and interest payments on the Authority's debt for the current fiscal year. It is funded through the revenue fund. The construction fund is established as a depository to pay all capital construction costs incurred by the City and reimbursed by the Authority. It is funded through the proceeds of bond and note sales. The escrow fund is established as a depository to refund debt in the future in future years. It is funded through bond proceeds.

**12 COMMITMENTS AND CONTINGENCIES****Construction**

The System has contractual commitments of approximately \$4,483 and \$4,197 million at June 30, 2004 and June 30, 2003, respectively, for water and sewer projects.

## Notes to Financial Statements, June 30, 2003 and 2004

(with summarized financial information for the year ended June 30, 2003)

### Claims and Litigation

In accordance with the Lease, the Board is required to reimburse the City for any judgment or settlement paid by the City arising out of a tort claim to the extent that the City's liability is related to capital improvements and the operation or maintenance of the System. However, in no event shall the payment made to the City, in any fiscal year, exceed an amount equal to 5% of the aggregate revenues shown on the prior year audited financial statements of the System. In addition, the System is required to reimburse the City, to the extent requested by the City, for the payment of any judgment or settlement arising out of a contract claim with respect to the construction of capital improvements. In addition, the City has agreed, subject to certain conditions, to indemnify the Authority, the Board and their staffs against any and all liability in connection with any act done or omitted in the exercise of their powers which is taken or omitted in good faith in pursuance of their purposes under the Act. Currently, the City is a defendant in a significant number of lawsuits pertaining to the System. The litigation includes, but is not limited to, actions commenced and claims asserted against the City arising out of alleged torts, alleged breaches of contract, condemnation proceedings and other alleged violations of law. As of June 30, 2004, the potential future liability attributable to the System for claims outstanding against the City was estimated to be \$131 million. This amount is included in the estimated liability for unsettled claims, which is reported in the City's balance sheet. The potential future liability is the City's best estimate based on available information. The estimate may be revised as further information is obtained and as pending cases are litigated.

### Arbitrage Rebate

To maintain the exemption from Federal income tax of interest on bonds issued subsequent to January 1, 1986, the System will fund amounts required to be rebated to the Federal Government pursuant to Section 148 of the Internal Revenue Code of 1986, as amended ("the Code"). The Code requires the payment to the United States Treasury of the excess of the amount earned on all non-purpose obligations over the amount that would have been earned if the gross proceeds of the issue were invested at a rate equal to the yield on the issue, together with any earnings attributable to such excess. Construction funds, debt service funds or any other funds or accounts funded with proceeds of such bonds, including earnings, or pledged to or expected to be used to pay interest on such bonds are subject to this requirement.

Payment is to be made after the end of the fifth bond year and after every fifth bond year thereafter, and within 60 days after retirement of the bonds. During 2004 and 2003 the System paid \$1 million and \$477 thousand, respectively, in rebates. At June 30, 2004 the Authority had a liability of \$4.745 million and had no liability at June 30, 2003.

### 13 POST EMPLOYMENT BENEFITS AND PENSION PLANS

The employees of the System are covered under the pension plans of the City. The employer's cost for these plans has been allocated to the System under the Operations and Maintenance expense.

### 14 PRIOR PERIOD ADJUSTMENTS

The 2003 financial statements have been restated, from the amounts previously reported, to reflect adjustments to utility plant in service and utility plant construction. Certain amounts previously reported as utility plant construction were placed into service in prior years and should have been reclassified to utility plant in service and depreciated accordingly. In addition, certain amounts included in utility plant construction should have been expensed in 2003 and in prior years. The effects of these adjustments to the 2003 financial statements are as follows: Utility plant in service, net of accumulated depreciation was increased by \$658 million. Utility plant construction was reduced by \$1.49 billion. Net assets at the beginning of the year were reduced by \$785 million and net assets at the end of the year were reduced by \$836 million, which included an adjustment to increase 2003 operation and maintenance expense and depreciation expense by \$26 million and \$25 million respectively. Net income before capital contribution was reduced by \$51 million.

### 15 SUBSEQUENT EVENTS

On August 5, 2004, the Authority issued fiscal 2005 Series A First Resolution Bonds in the aggregate amount of \$150 million to reimburse outstanding commercial paper notes, to pay certain costs of issuance, and to fund certain reserves.

On August 11, 2004, the Authority issued Fiscal 2005 Series 1 Second Resolution Bonds in the aggregate amount of \$230.4 million, to reimburse outstanding commercial paper notes, and to pay certain costs of issuance.

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**FORM OF OPINION OF BOND COUNSEL  
(Fiscal 2006 Series AA Bonds)**

October 18, 2005

New York City Municipal  
Water Finance Authority

**New York City Municipal Water Finance Authority  
Water and Sewer System Second General Resolution Revenue Bonds,  
Fiscal 2006 Series AA  
(Final Opinion)**

Ladies and Gentlemen:

We have acted as bond counsel in connection with the issuance by the New York City Municipal Water Finance Authority (the "Authority"), a body corporate and politic constituting a public benefit corporation of the State of New York (the "State"), created and existing under and pursuant to the Constitution and statutes of the State, including the Act (defined below), of \$400,000,000 aggregate principal amount of Water and Sewer System Second General Resolution Revenue Bonds, Fiscal 2006 Series AA (the "2006 Series AA Bonds"), issued under and pursuant to the New York City Municipal Water Finance Authority Act, being Title 2-A of Article 5 of the Public Authorities Law of the State, as amended (which, together with Section 1046 of the Public Authorities Law of the State, is herein referred to as the "Act") and a resolution of the Authority adopted March 30, 1994 entitled "Water and Sewer System Second General Revenue Bond Resolution," as amended and supplemented to the date hereof (the "Resolution"), including by a supplemental resolution adopted September 26, 2005 entitled Thirty-Seventh Supplemental Resolution "Authorizing the Issuance of Water and Sewer System Second General Resolution Revenue Bonds, Fiscal 2006 Series AA" (the "Thirty-Seventh Supplemental Resolution") authorizing the 2006 Series AA Bonds. The 2006 Series AA Bonds are part of an issue of bonds of the Authority (the "Bonds") which the Authority has created under the terms of the Resolution and is authorized to issue from time to time for the purposes authorized by the Act and the Resolution, as then in effect, and without limitation as to amount except as provided in the Resolution or as may be limited by law. The 2006 Series AA Bonds are being issued for the purposes of the Resolution. Capitalized terms not otherwise defined herein shall have the meanings ascribed thereto in the Resolution.

Pursuant to the Act, the New York City Water Board (the "Board"), a public benefit corporation of the State, created and existing under the laws of the State, and The City of New York (the "City"), a municipal corporation of the State, have entered into a lease agreement, dated as of July 1, 1985, as amended (the "Lease"), whereby the Board has leased the New York City Water and Sewer System from the City for a term ending on the date on which all bonds, notes or other obligations of the Authority have been paid in full or provision for such payment shall have been made in accordance with the instruments under which they were issued. Pursuant to the Act, the Authority, the Board and the City have entered into a financing agreement, dated July 1, 1985, as amended (the "Financing Agreement"), related to, among other things, the financing Water Projects.

In such connection, we have reviewed the Resolution, the Thirty-Seventh Supplemental Resolution, the Authority's Water and Sewer System General Revenue Bond Resolution, adopted November 14, 1985 (the "First Resolution"), the Lease, the Financing Agreement, the Tax Certificate of the Authority (the "Tax Certificate"), opinion of Corporation Counsel of The City of New York, certificates of the Authority, the Trustee and others, and such other documents, opinions and matters to the extent we deemed necessary to render the opinions set forth herein.

Certain agreements, requirements and procedures contained or referred to in the Resolution, the Thirty-Seventh Supplemental Resolution, the First Resolution, the Lease, the Financing Agreement, the Tax Certificate and other relevant documents may be changed and certain actions (including, without

limitation, defeasance of 2006 Series AA Bonds) may be taken or omitted under the circumstances and subject to the terms and conditions set forth in such documents. No opinion is expressed herein as to any 2006 Series AA Bond or the interest thereon if any such change occurs or action is taken or omitted upon the advice or approval of counsel other than ourselves.

The opinions expressed herein are based on an analysis of existing laws, regulations, rulings and court decisions and cover certain matters not directly addressed by such authorities. Such opinions may be affected by actions taken or omitted or events occurring after the date hereof. We have not undertaken to determine, or to inform any person, whether any such actions are taken or omitted or events do occur or any other matters come to our attention after the date hereof, and we disclaim any obligation to update this letter. We have assumed the genuineness of all documents and signatures presented to us (whether as originals or as copies) and the due and legal execution and delivery thereof by, and validity against, any parties other than the Authority. We have assumed, without undertaking to verify, the accuracy of the factual matters represented, warranted or certified in the documents, and of the legal conclusions contained in the opinions, referred to in the third paragraph hereof. Furthermore, we have assumed compliance with all covenants and agreements contained in the Resolution, the Supplemental Resolution, the Lease, the Financing Agreement and the Tax Certificate, including (without limitation) covenants and agreements compliance with which is necessary to assure that future actions, omissions or events will not cause interest on the 2006 Series AA Bonds to be included in gross income for federal income tax purposes. We call attention to the fact that the rights and obligations under the 2006 Series AA Bonds, the Resolution, the Supplemental Resolution, the First Resolution, the Lease, the Financing Agreement and the Tax Certificate and their enforceability may be subject to bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting creditors' rights, to the application of equitable principles and to the exercise of judicial discretion in appropriate cases. We express no opinion with respect to any indemnification, contribution, penalty, choice of law, choice of forum or waiver provisions contained in the foregoing documents, nor do we express any opinion with respect to the state or quality of title to or interest in any of the real or personal property described in or as subject to the lien of the Resolution, the Supplemental Resolution, the First Resolution, the Lease or the Financing Agreement, or the accuracy or sufficiency of the description contained therein of, or the remedies available to enforce liens on, any such property. Finally, we undertake no responsibility for the accuracy, completeness or fairness of the Official Statement or other offering material relating to the 2006 Series AA Bonds and express no opinion with respect thereto herein.

Based on and subject to the foregoing, and in reliance thereon, as of the date hereof we are of the following opinions:

1. The Authority is a body corporate and politic constituting a public benefit corporation of the State, duly created and existing under the laws of the State with the right and lawful authority and power to enter into the Financing Agreement, to adopt the Resolution and the Supplemental Resolution and to issue the 2006 Series AA Bonds.

2. The Resolution and the Supplemental Resolution have been duly and lawfully adopted by the Authority, are in full force and effect and are the legal, valid and binding agreements of the Authority enforceable in accordance with their terms. The Resolution and the Supplemental Resolution create the valid, binding and perfected pledges they purport to create of the Revenues and any moneys or securities on deposit in the Funds and Accounts created thereby for the repayment of the Bonds, subject only to the provisions of the Resolution, the Supplemental Resolution and the Financing Agreement permitting the application thereof for or to the purposes and on the terms and conditions permitted thereby, including the making of any required payments to the United States with respect to arbitrage earnings.

3. The 2006 Series AA Bonds have been duly and validly authorized and issued. The 2006 Series AA Bonds are valid and binding special obligations of the Authority payable as provided in the Resolution, are enforceable in accordance with their terms and the terms of the Resolution and are entitled, together with all other Bonds issued under the Resolution to the benefits of the Resolution and the Act.



4. The 2006 Series AA Bonds are payable solely from the Revenues and other amounts pledged to such payment under the Resolution. The 2006 Series AA Bonds are not a debt of the State, the City or the Board and neither the State, the City, the Board nor any other political subdivision of the State is liable thereon.

5. The Lease and the Financing Agreement have been duly authorized, executed and delivered by the respective parties thereto and constitute valid and binding obligations of such parties, enforceable in accordance with their terms.

6. The Revenues derived from the operation of the System are the property of the Board. The Financing Agreement validly transfers the right, title and interest of the Board in the Revenues to the Authority to the extent and as provided in the Financing Agreement, subject only to the provisions of the Act, the Financing Agreement and the Resolution permitting the application thereof for or to the purposes, and on the terms and conditions, therein set forth.

7. By virtue of the Act, the Authority has a valid, binding and perfected statutory lien upon the Revenues to be paid by the Board to the Authority pursuant to the Financing Agreement and such lien constitutes a first priority security interest therein.

8. Interest on the 2006 Series AA Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986. Interest on the 2006 Series AA Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although we observe that it is included in adjusted current earnings when calculating corporate alternative minimum taxable income. Interest on the 2006 Series AA Bonds is exempt from personal income taxes imposed by the State of New York and any political subdivision thereof (including The City of New York). We express no opinion regarding other tax consequences related to the ownership or disposition of, or the accrual or receipt of interest on, the 2006 Series AA Bonds.

In rendering the opinions set forth in paragraphs 5 and 6 above, we wish to advise you that we have, with your consent, relied upon the opinion of Corporation Counsel of The City of New York dated the date hereof and addressed to you as to the validity, binding effect and enforceability of the Lease and the Financing Agreement with respect to the Board and the City. In rendering the priority of lien opinion set forth in paragraph 7 above, we have (i) relied upon a certification by the Board that it has not made or granted a pledge of or security interest in the Revenues to any person other than the Authority and that it has not taken any action which could result in the imposition by operation of law of any lien, charge or encumbrance upon the Revenues, and (ii) assumed, without making any independent investigation, that (1) no lien, charge or encumbrance upon the Revenues has been imposed or exists by operation of law that is prior to the lien in favor of the Authority and (2) no facts or circumstances have occurred or exist which could result in the imposition by operation of law of any lien, charge or encumbrance upon the Revenues that is prior to the lien in favor of the Authority.

Faithfully yours,

ORRICK, HERRINGTON & SUTCLIFFE LLP

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**BOOK-ENTRY-ONLY FORM**

The Depository Trust Company (“DTC”), New York, NY, will act as securities depository for the Fiscal 2006 AA Bonds. The Fiscal 2006 AA Bonds will be issued as fully-registered securities registered in the name of Cede & Co. (DTC’s partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered bond certificate will be issued for each maturity of the Fiscal 2006 AA Bonds, each in the aggregate principal amount of such maturity, and will be deposited with DTC, in the aggregate principal amount of the Fiscal 2006 AA Bonds, and will be deposited with DTC.

DTC is a limited-purpose trust company organized under the New York Banking Law, a “banking organization” within the meaning of the New York Banking Law, a member of the Federal Reserve System, a “clearing corporation” within the meaning of the New York LLC Uniform Commercial Code, and a “clearing agency” registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 2 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments from over 85 countries that DTC’s participants (“Direct Participants”) deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants’ accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (“DTCC”). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Government Securities Clearing Corporation, MBS Clearing Corporation, and Emerging Markets Clearing Corporation, (also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (“Indirect Participants”). The DTC Rules applicable to its Direct Participants and Indirect Participants (collectively, “Participants”) are on file with the Securities and Exchange Commission.

Purchases of Fiscal 2006 AA Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Fiscal 2006 AA Bonds on DTC’s records. The ownership interest of each actual purchaser of each Fiscal 2006 A Bond (“Beneficial Owner”) is in turn to be recorded on the Direct and Indirect Participants’ records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Fiscal 2006 AA Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in Fiscal 2006 AA Bonds, except in the event that use of the book-entry system for the Fiscal 2006 AA Bonds is discontinued.

To facilitate subsequent transfers, all Fiscal 2006 AA Bonds deposited by Direct Participants with DTC are registered in the name of DTC’s partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Fiscal 2006 AA Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of any Fiscal 2006 AA Bonds; DTC’s records reflect only the identity of the Direct Participants to whose accounts the Fiscal 2006 AA Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial

Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial Owners of Fiscal 2006 AA Bonds may wish to take certain steps to augment transmission to them of notices of significant events with respect to the Fiscal 2006 AA Bonds, such as redemptions, tenders, defaults and proposed amendments to the bond documents. For example, Beneficial Owners of Fiscal 2006 AA Bonds may wish to ascertain that the nominee holding the Fiscal 2006 AA Bonds for their benefit has agreed to obtain and transmit notices to Beneficial Owners. In the alternative, Beneficial Owners may wish to provide their names and addresses to the Bond Registrar and request that copies of notices be provided directly to them.

Redemption notices shall be sent to DTC. If less than all of the Fiscal 2006 AA Bonds within a maturity are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such maturity to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the Fiscal 2006 AA Bonds unless authorized by a Direct Participant in accordance with DTC's Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the Authority as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts the Fiscal 2006 AA Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal and interest payments on the Fiscal 2006 AA Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts, upon DTC's receipt of funds and corresponding detail information from the Authority or Trustee on the payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC (nor its nominee), the Trustee, or the Authority, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal, premium, if any, and interest on the Fiscal 2006 AA Bonds to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the Trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as depository with respect to the Fiscal 2006 AA Bonds at any time by giving reasonable notice to the Authority or the Trustee. Under such circumstances, in the event that a successor securities depository is not obtained, bond certificates are required to be printed and delivered.

The Authority may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, bond certificates will be printed and delivered.

Unless otherwise noted, the information contained in the preceding paragraphs of this subsection "Book-Entry-Only System" has been extracted from information given by DTC. Neither the Authority, the Trustee nor the Underwriters makes any representation as to the completeness or the accuracy of such information or as to the absence of material adverse changes in such information subsequent to the date hereto.

**NEITHER THE AUTHORITY NOR THE TRUSTEE WILL HAVE ANY RESPONSIBILITY OR OBLIGATIONS TO SUCH DTC PARTICIPANTS, INDIRECT PARTICIPANTS, OR THE PERSONS FOR WHOM THEY ACT AS NOMINEES WITH RESPECT TO THE PAYMENTS TO OR THE PROVIDING OF NOTICE FOR SUCH DTC PARTICIPANTS, INDIRECT PARTICIPANTS, OR THE BENEFICIAL OWNERS.**

**DESCRIPTION OF THE FACILITY PROVIDERS**

The Authority makes no representation as to the accuracy or adequacy of the information relating to the Facility Providers set forth below or as to the absence of material adverse changes in such information subsequent to the date indicated. Summaries of or references to the Credit Facilities are made subject to all the detailed provisions thereof to which reference is hereby made for further information and do not purport to be complete statements of any or all such provisions.

**AA-1 Facility Providers***State Street Bank and Trust Company*

State Street Bank and Trust Company (the “Bank”) is a wholly-owned subsidiary of State Street Corporation (the “Corporation”). The Corporation (NYSE: STT) is a leading specialist in providing institutional investors with investment servicing, investment management and investment research and trading. With \$9.5 trillion in assets under custody and \$1.4 trillion in assets under management, the Corporation operates in 25 countries and more than 100 markets worldwide. The assets of the Bank at December 31, 2004 accounted for approximately 96% of the consolidated assets of the Corporation. At December 31, 2004, the Corporation had total assets of \$94.040 billion, total deposits (including deposits in foreign offices) of \$55.129 billion, total loans and lease finance assets net of unearned income, allowance and reserve for possible credit losses of approximately \$4.611 billion and total equity capital of \$6.159 billion.

The Bank’s Consolidated Reports of Condition for Insured Commercial and State Chartered Savings Banks FFIEC 031 for December 31, 2004, as submitted to the Federal Reserve Bank of Boston, are incorporated by reference in this Appendix and shall be deemed to be a part hereof.

In addition, all reports filed by the Bank pursuant to 12 U.S.C. §324 after the date of this Official Statement shall be deemed to be incorporated herein by reference and shall be deemed to be a part hereof from the date of filing of any such report.

Additional information, including financial information relating to the Corporation and the Bank is set forth in the Corporation’s Annual Report or Form 10-K for the year ended December 31, 2004. The annual report can be found on the Corporation’s web site, [www.statestreet.com](http://www.statestreet.com). Such report and all reports filed by the Corporation pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, after the date of this Official Statement are incorporated herein by reference and shall be deemed a part hereof from the date of filing of any such report. The AA-1 Standby Purchase Agreement is an obligation of the Bank and not of the Corporation.

Any statement contained in any document incorporated or deemed to be incorporated by reference herein shall be deemed to be modified or superseded for purposes of this Official Statement to the extent that a statement contained herein or in any subsequently filed document that also is or is deemed to be incorporated by reference herein modifies or supersedes such statement. Any statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this Official Statement.

The Bank hereby undertakes to provide, without charge to each person to whom a copy of this has been delivered, on the written request of any such person, a copy of any or all of the documents referred to above which have been or may be incorporated in this by reference, other than exhibits to such documents. Written requests for such copies should be directed to Investor Relations, State Street Corporation, One Lincoln Street, Boston, Massachusetts 02111, telephone number 617-786-3000.

Neither the Bank nor its affiliates make any representation as to the contents of this Official Statement (except as to this Appendix to the extent it relates to the Bank), the suitability of the Fiscal 2006 AA Bonds for any investor, the feasibility or performance of any project or compliance with any securities or tax laws or regulations.

## *California State Teachers' Retirement System*

CALSTRS is a component unit of the State of California (the "State"), organized and operating under the laws of the State, including the Teachers' Retirement Law, constituting Part 13 of Division 1 of Title 1 of the Education Code of the State, commencing at Section 22000 (the "Law"), as amended. The Law establishes the Teachers' Retirement Board (the "Board"), which has the sole and exclusive fiduciary responsibility over the administration and investment of funds held in the Teachers' Retirement Fund (the "Fund"), in which the bulk of the assets of CALSTRS are held. School districts and other agencies employing members of CALSTRS are required to make monthly contributions to the Fund in an amount equal to 8.25% of the total of the salaries upon which members' contributions are based. All full-time certificated employees in the public school system from kindergarten through the community college level are required by law to be members of CALSTRS. CALSTRS provides defined retirement, survivor and disability benefits to all members based on the final compensation attained by the member, the age of retirement and the term of service, and other factors.

Financial data for June 30, 2004 are taken from the audited financial statements presented in CALSTRS' Comprehensive Annual Financial Report ("Annual Report") for the fiscal year ended June 30, 2004.

As of June 30, 2004, the Fund had net assets held in trust for pension benefits with a market value of approximately \$116.1 billion, compared to approximately \$100.4 billion as of June 30, 2003. As of August 31, 2005, net assets had a total market value of approximately \$132.7 billion (unaudited).

CALSTRS is independently rated "AA+/A-1+" by Standard and Poor's, a Division of the McGraw-Hill Companies, Inc. ("S&P"), "Aaa/VMIG1" by Moody's Investors Service, and "AAA/F-1+" by Fitch Ratings.

CALSTRS will provide without charge, upon request, a copy of the 2004 Annual Report containing its financial statements for the years ended June 30, 2004 and 2003. Requests to CALSTRS for the Annual Report should be directed by mail or phone to State Teachers' Retirement System, P.O. Box 163740, Sacramento, California 95816-3710, Attention: Credit Enhancement Program, or by email address to [cepinquiries@calstrs.com](mailto:cepinquiries@calstrs.com). The most recent Annual Report and other information regarding CalSTRS can be viewed at [www.calstrs.com](http://www.calstrs.com).

**The foregoing information has been provided by CALSTRS and is not intended to serve as a representation, warranty, or contract modification of any kind.**

### **AA-2 and AA-3 Facility Provider**

#### *Dexia Crédit Local*

Dexia Crédit Local ("Dexia") is a subsidiary of the Dexia Group, which was created in 1996. The Dexia Group is a major European banking organization that is the product of several cross-border mergers. Dexia is an authentically European bank in terms of both its management organization and the scope of its different lines of business. The Dexia Group is listed on the Brussels, Paris and Luxembourg stock exchanges. With a stock market capitalization of over 19 billion euros as of December 31, 2004, the Dexia Group ranks in the top third of the Euronext 100 companies.

Dexia specializes in the Dexia Group's first line of business – public and project finance and financial services for the public sector. Dexia has recognized expertise in local public sector financing and project finance. It is backed by a network of specialized banks, which employ over 3,000 professionals. Through this network of subsidiaries, affiliates and branches, Dexia is present in almost all of the countries of the European Union as well as Central Europe, the United States of America and Canada. Dexia also has operations in Latin America, the Asian-Pacific Region including Australia, and the countries around the Mediterranean.

Dexia is a bank with its principal office located in Paris, France. In issuing the facility, Dexia will act through its New York Branch, which is licensed by the Banking Department of the State of New York as

an unincorporated branch of Dexia Credit Local, Paris. Dexia is the leading local authority lender in Europe, funding its lending activities in 2004 primarily through the issuance of euro and U.S. dollar-denominated bonds. In 2004, total funding raised by Dexia and Dexia Municipal Agency was 11.7 billion euros.

The Dexia Group is the owner of Financial Security Assurance Holdings Ltd. (“FSA Holdings”), the holding company for Financial Security Assurance Inc., a leading financial guaranty insurer.

As of December 31, 2004, Dexia had total consolidated assets of 206.0 billion euros, outstanding medium and long-term loans to customers of 168.13 billion euros and shareholders’ equity of over 4.32 billion euros (Tier I plus Tier II), and for the year then ended had consolidated net income of 705 million euros. These figures were determined in accordance with generally accepted accounting principles in France. Dexia maintains its records and prepares its financial statements in euros. At December 31, 2004, the exchange rate was 1.0000 euro equals 1.3621 United States dollar. Such exchange rate fluctuates from time to time.

Dexia is rated Aa2 long-term and P-1 short-term by Moody’s, AA long-term and A-1+ short-term by S&P, and AA+ long-term and F1+ short-term by Fitch.

Dexia will provide without charge a copy of its most recent publicly available annual report. Written requests should be directed to: Dexia Credit Local, New York Branch, 445 Park Avenue, 7th Floor, New York, New York 10022, Attention: General Manager. The delivery of this information shall not create any implication that the information contained or referred to herein is correct as of any time subsequent to its date.

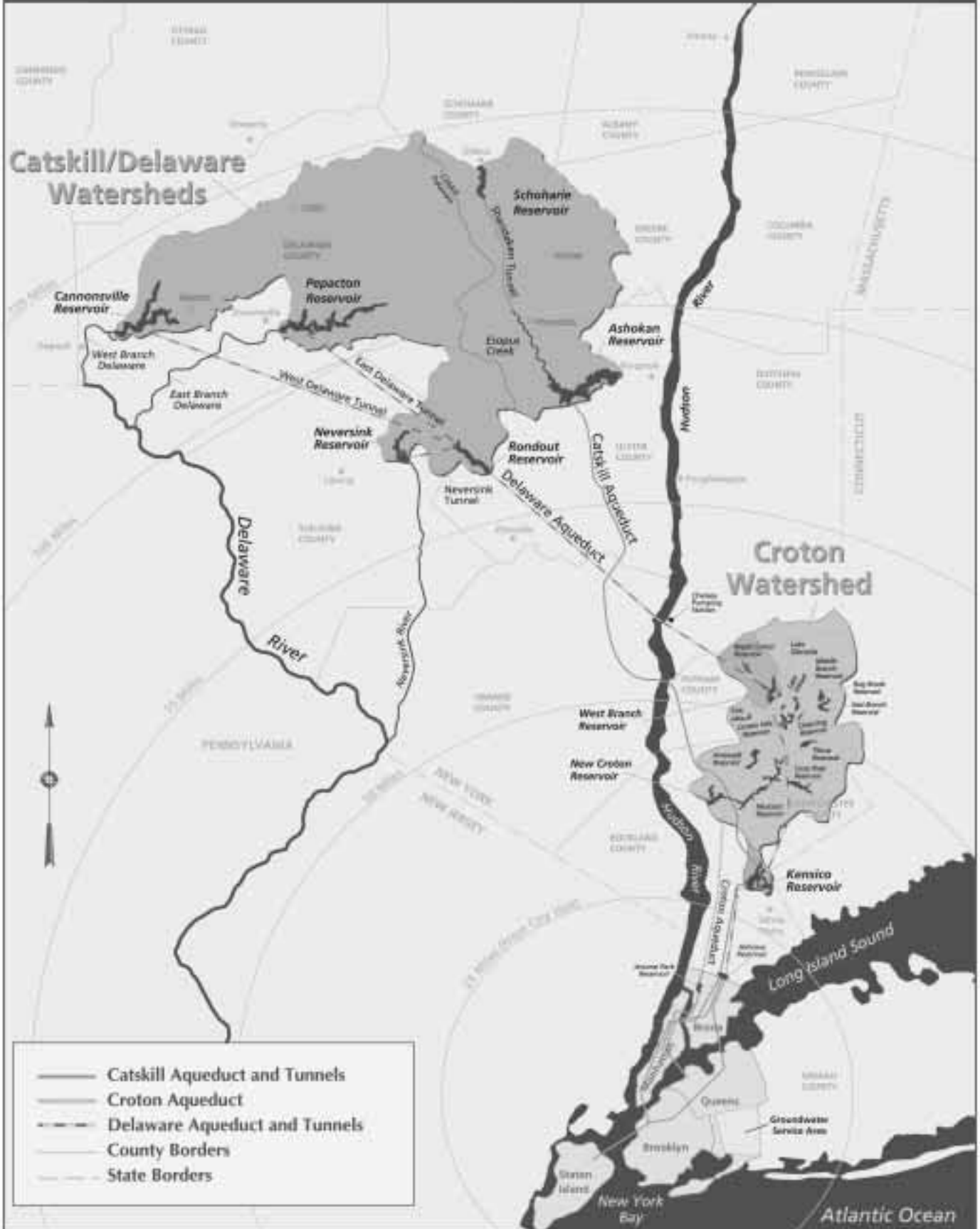
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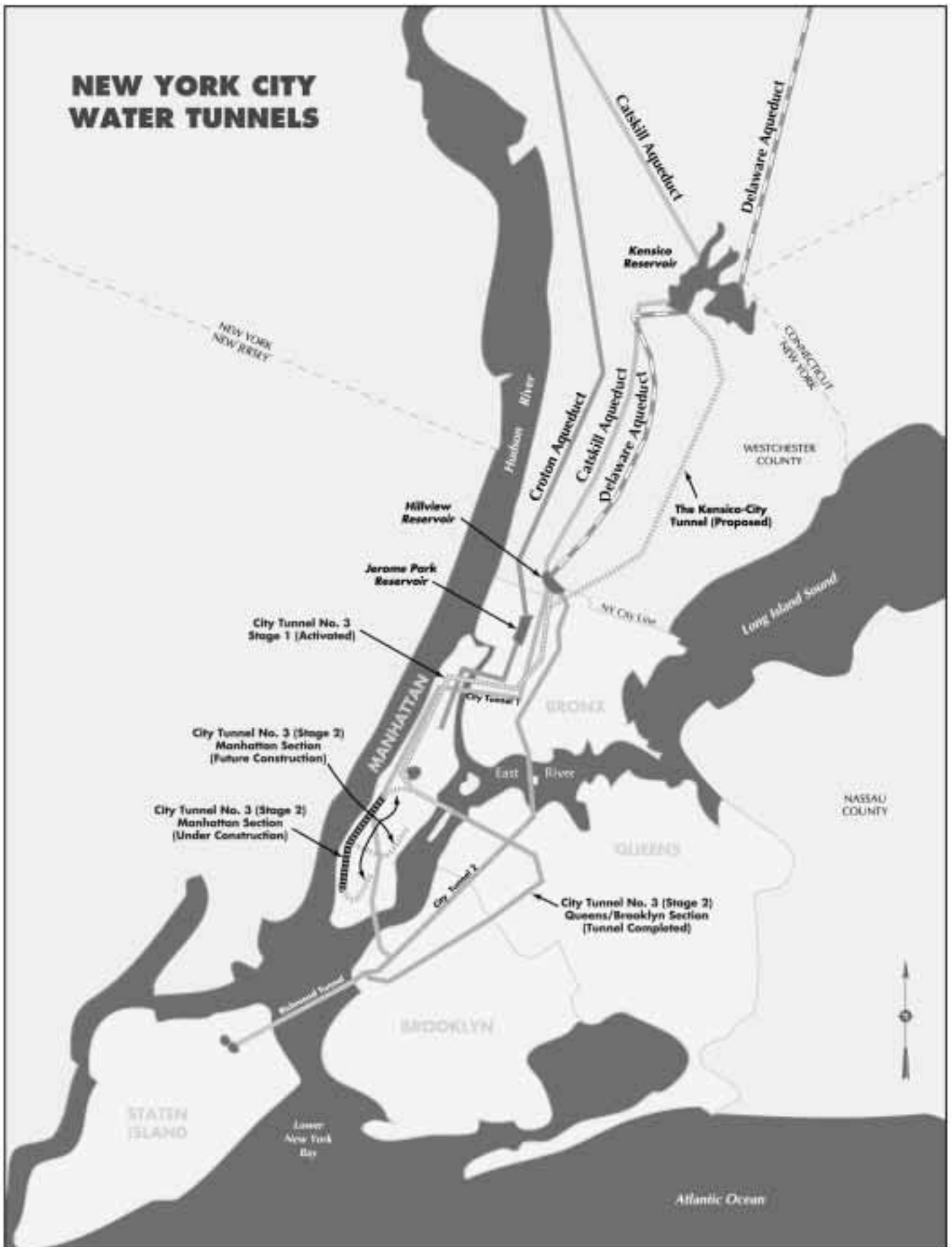
**SYSTEM MAPS**

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# New York City Water Supply System



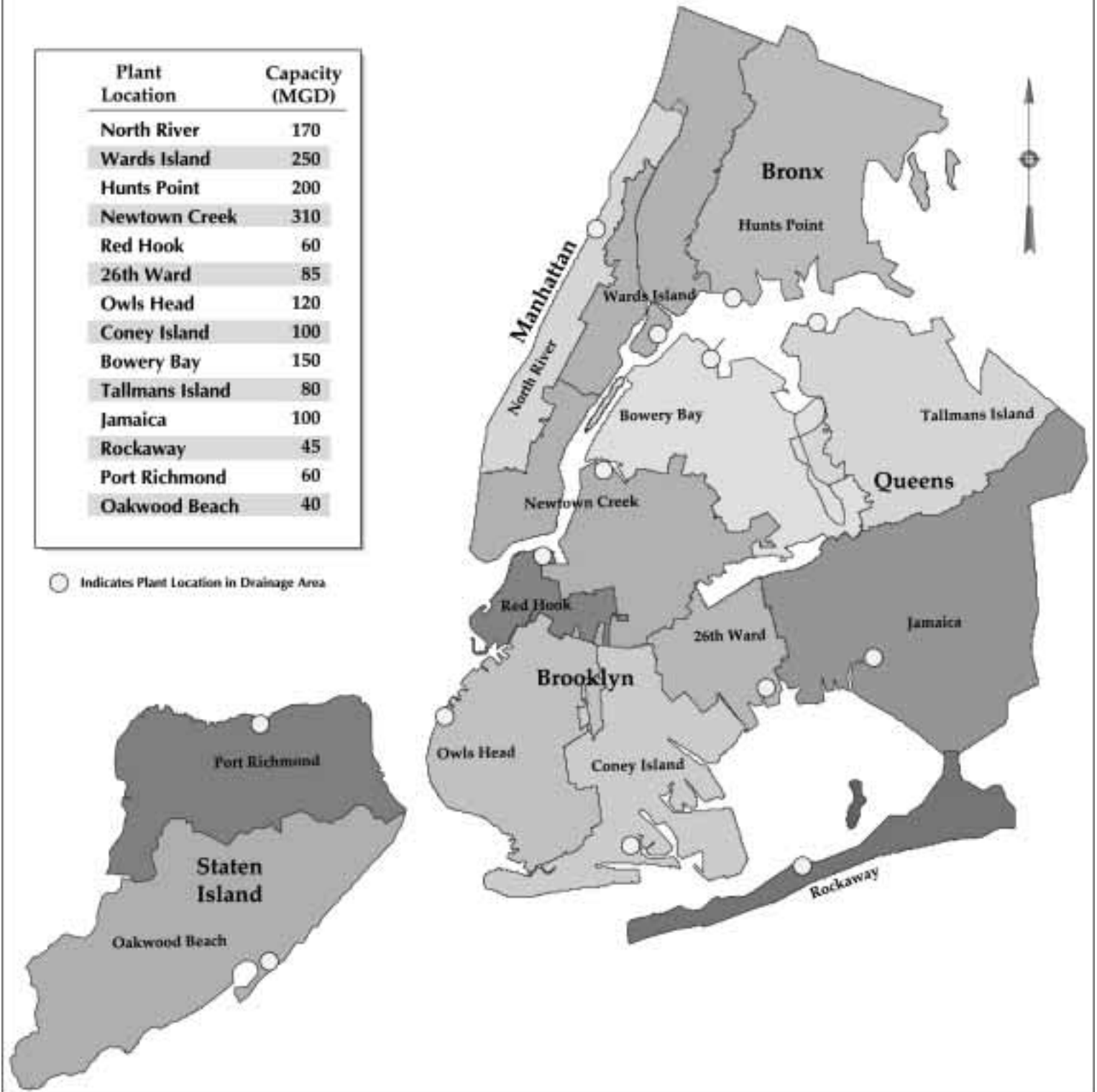
# NEW YORK CITY WATER TUNNELS



# New York City Drainage Areas and Water Pollution Control Plants

Plant Location	Capacity (MGD)
North River	170
Wards Island	250
Hunts Point	200
Newtown Creek	310
Red Hook	60
26th Ward	85
Owls Head	120
Coney Island	100
Bowery Bay	150
Tallmans Island	80
Jamaica	100
Rockaway	45
Port Richmond	60
Oakwood Beach	40

○ Indicates Plant Location in Drainage Area



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